

A study on how franchisees finance their owner's contribution when buying a franchise

A Dissertation
presented to

The Development Finance Centre (DEFIC)
Graduate School of Business
University of Cape Town

In partial fulfilment of
the requirements for the
Master of Commerce in Development Finance Degree

By

Lumka Ngqola-Sebone

October 2019

Supervisor: Dr Badri Zolfaghari

Co-Supervisor: Dr Abdul Latif Alhassan

The copyright of this thesis vests in the author. No quotation from it or information derived from it is to be published without full acknowledgement of the source. The thesis is to be used for private study or non-commercial research purposes only.

Published by the University of Cape Town (UCT) in terms of the non-exclusive license granted to UCT by the author.

PLAGIARISM DECLARATION

Declaration

1. I know that plagiarism is wrong. Plagiarism is to use another's work and pretend that it is one's own.
2. I have used the APA convention for citation and referencing. Each contribution to and quotation in, this study "A **study on how franchisees finance their owner's contribution when buying a franchise**" from the work(s) of other people has been attributed and has been cited and referenced.
3. This dissertation is my own work.
4. I have not allowed and will not allow, anyone to copy my work with the intention of passing it off as his or her own work.
5. I acknowledge that copying someone else's assignment or essay, or part of it, is wrong and declare that this is my own work.

Signature

Name: Ms. Lumka Ngqola-Sebone

ABSTRACT

The South African economy has been lagging its forecasted economic growth statistics in recent years, particularly following the worldwide economic recession of 2008. The year-on-year economic growth of South Africa is forecasted to continue to be lower than other developing countries. SMMEs are a significant contributor to a countries GDP and most franchises are classified as SMMEs. Entrepreneurs in the SMME space often use franchises to not only penetrate the market but to grow existing ventures. In its annual report for the year 2016, the Franchise Association of South Africa (FASA) states that the franchise industry contributed an estimated 11.6% to South Africa's GDP.

When applying for finance at most institutions, prospective franchisees are required to also contribute to the total funding required; this is known as owner's contribution. This study explores what challenges franchisees experience in trying to raise owners' contribution and how they overcame these challenges. It further explores what prospective franchisees can learn from the experiences of the participants.

Through research conducted predominantly through an online survey and interviews to a limited extent, this study found that the franchise model has many advantages, but also has disadvantages. One of the main disadvantages remains the accessibility of finance, particularly that most financiers and franchisors require substantial owners' contribution. Many participants faced challenges when having to raise owner's contribution

They most used personal savings and donations or borrowings from friends and family. The negative impacts that were identified were mainly personal stress and anxiety, strained personal relationships and delays in personal and/or business plans.

In conclusion, in attempting to address these challenges highlighted by participants, recommendations are made to all stakeholders on how to overcome some of the challenges identified.

TABLE OF CONTENTS	Page
PLAGIARISM DECLARATION	i
ABSTRACT	ii
TABLE OF CONTENTS	Page iii
GLOSSARY OF TERMS AND ABBREVIATIONS	vi
ACKNOWLEDGEMENTS	viii
CHAPTER ONE: INTRODUCTION	1
1.1 Introduction of the research area	1
1.1.1 Criteria required in order to qualify as a franchisee or to own a franchise	3
1.2 Problem statement	5
1.2.1 Franchisee’s owners’ equity requirement	7
1.3 The aim and objectives of the study	8
1.4 Research questions and scope	8
1.5 Purpose and significance of the research.....	9
1.6 Conclusion and overview of chapters.....	9
CHAPTER TWO: LITERATURE REVIEW	11
2.1 Introduction	11
2.2 Background on franchises	11
2.3 Franchising defined	12
2.4 Overview of the franchise industry in South Africa.....	12
2.5 Why entrepreneurs choose franchising	13
2.6 Definition of a successful franchisee and key franchisee attributes	14
2.7 Cost of franchises in South Africa.....	15
2.8 Source of finance for a start-up franchise.....	16
2.9 Capital structure theories	20
2.10 Optimal capital structure for a start-up franchise	22
2.11 Sources of owners’ equity	22
2.11.1 Own resources or savings	23
2.11.2 Angel investors	23
2.11.3 Friends and family	23
2.12 Commitment levels.....	24
2.13 Conclusion.....	24
CHAPTER THREE: RESEARCH METHODOLOGY.....	25
3. Introduction	25

3.1	Research approach and strategy	25
3.1.1	Qualitative research	25
3.2	Research design.....	26
3.3	Data collection.....	26
3.3.1	Online questionnaire	27
3.3.2	Interviews with participants, franchisors, franchise associations and financiers	28
3.3	Sampling.....	28
3.4	Data analysis methods	30
3.4.1	Quantitative data analysis	30
3.4.2	Qualitative data analysis	31
3.5	Research reliability and validity	31
3.7	Limitations	32
3.8	Chapter summary	33
CHAPTER FOUR: RESEARCH FINDINGS, ANALYSIS AND DISCUSSION		34
4	Introduction	34
4.1	Demographics of participants.....	34
4.2	Sectors that participants first franchise operates in	35
4.3	South African province in which the franchise operates in.....	37
4.4	Length of time of the franchise operation	38
4.5	Financing of the franchise	39
CHAPTER FIVE: RESEARCH CONCLUSIONS AND RECOMMENDATIONS		50
5.	Introduction	50
5.1	Summary of findings and conclusion of study	50
5.1.1	Unencumbered equity requirements	50
5.1.2	Sources of unencumbered equity contribution and the implications thereof	51
5.2	Stakeholder recommendations	51
5.2.1	Practical recommendations	51
5.2.2	Policy recommendations	53
5.2.3	Recommendations for future research	53
5.2.3.1	One-on-one, face-to-face interviews of franchisees	53
5.2.3.2	Questionnaire inclusive of all nine provinces of South Africa	54
5.3	Conclusion.....	54
REFERENCES		55
APPENDICES.....		63

Appendix A: Online questionnaire that research participants completed	63
Appendix B: Tables.....	67
Table 1: Origins of franchised systems operating in South Africa in 2004.....	67
Table 2: Franchise industry sector.....	67
Table 3: Sorbet start-up costs (Source: Sorbet website).....	68
Appendix C: Figures	69
Figure 1: The South African and global economic year on year growth, 2010-2023- 2016.....	69
Figure 2: The South African unemployment rate.....	69
Figure 3: Key challenges facing entrepreneurs according to The Seed Academy 2016 start-up survey	70
Figure 4: How entrepreneurs funded their business to date according to The Seed Academy 2016 start-up survey	70
Figure 5: Franchisees annual turnover.....	71
Figure 6: Franchisees time in business.....	71

GLOSSARY OF TERMS AND ABBREVIATIONS

CFS	Criteria for Success
Collateral	something pledged as security for repayment of a loan, to be forfeited in the event of a default.
DFI	Development Finance Institution
DTI	The Department of Trade and Industry
FASA	Franchise Association of South Africa
Franchise	a right to sell a company's products in a particular area using the company's name
Franchisee	An individual or company that holds a franchise for the sale of goods or the operation of a service.
Franchisor	The company that allows an individual (known as the franchisee) to run a location of their business. The franchisor owns the overarching company, trademarks and products, but gives the right to the franchisee to run the franchise location, in return for an agreed-upon fee
GDP	Gross Domestic Product
IDC	Industrial Development Corporation of South Africa
KPI's	Key Performance Indicators
Liquidate	To liquidate means to convert assets into cash or cash equivalents by selling them on the open market. Liquidate is also a term used in bankruptcy procedures in which an entity chooses or is forced by a legal judgment or contract to turn assets into a "liquid" form (cash). In finance, an asset is an item that has value.
Liquidation	The process of converting assets into cash
NEF	National Empowerment Fund
Participant(s)	The franchisees that participated in the questionnaire that this research paper is based on
SME	Small and medium-sized enterprises
SMME	Small, medium and micro enterprises
Surety	a person who takes responsibility for another's performance of an undertaking, for example their appearing in court or paying a debt.

susu	<p>Susu is a method of pooling savings in parts of West Africa and the Caribbean</p> <p>A group of people regularly pays a fixed sum into a pool held by a Susu collector. Each time group members contribute, one of them receives the entire sum. Thus, if 20 people each contribute 10 dollars per week, every one of them will receive 200 dollars at a certain point in time</p>
------	---

ACKNOWLEDGEMENTS

I would firstly like to thank my Creator for giving me the strength, wisdom and resources that were required to do this work, without whom it would not have been possible.

To my supportive and loving husband, thank you Ntate Sebone for proofreading my many drafts when you could have been watching or playing soccer. I'm truly blessed to have you.

To my sweet boys, thank you for understanding when mommy could not play with you as often, I love you.

To my wonderful family and friends, thank you for hanging in there and encouraging me through the long days and sleepless nights, it has all finally paid off.

I would also like to express my appreciation to my supervisors, your guidance throughout the gruelling process of completing this dissertation was appreciated. I would not have been able to do this without you.

Lastly, I would like to express my sincere gratitude to the individuals that took part in this study by participating in the questionnaire that I distributed and answering my emails, calls and texts. Thank you for taking time out from your schedules to not only assist me in completing this study but also to assist other stakeholders with an interest in franchising with much needed information by adding to the body of knowledge that currently exists on the subject matter.

CHAPTER ONE: INTRODUCTION

1.1 Introduction of the research area

Franchises and franchising have been proven to be a great avenue for many entrepreneurs looking to start-up or to expand their business. There are however a lot of barriers that entrepreneurs must overcome to make their business venture a reality. This chapter serves to provide a brief background to SMME and Franchise finance. It further provides some insight on how franchisees raised *equity* funding for the purchase of their franchises and the challenges they faced in raising said funding.

The Franchise Association of South Africa (FASA) states that the franchise industry contributes an estimated 12.5% to South Africa's GDP (<http://www.fasa.co.za/>). Entrepreneurs in the SMME space often use franchises to not only penetrate the market but to grow existing ventures. Macleod (1999) states that opening a franchise is one of the best opportunities for aspiring entrepreneurs. He lists various advantages for going the franchise route (these are discussed later in this paper) and concludes that in the end, the advantages of opening a franchise far outweigh the disadvantages.

Franchising has enjoyed good reviews in South Africa for several year's running. SA- The Good News website has stated that "According to the International Franchise Association (IFA), despite slower than expected growth in 2014, so far, the outlook for franchise growth remains strong with employment and output forecasts revised up slightly from January estimates" (IHS Economics, (2014), pg. 1).

The South African economy has been lagging its forecasted economic growth statistics in recent years, particularly following the worldwide economic recession of 2008. The year-on-year economic growth of South Africa is forecasted to continue to be lower than other developing countries as seen in Appendix C: Figure 1, on page 67 of this report (National Treasury Budget Review, 2019). Developing countries gross domestic product (GDP) growth rates (dotted red line) are higher than other economies as can be expected. South Africa is classified as a developing country and should as a result be performing at the same levels, all things being equal. Since the year 2000 South Africa's GDP has been growing at levels lower than other developing countries, in addition and of concern is that in the first quarter of 2016 the GDP growth rate has contracted by 1.2%. Whilst NKC Economics (2017) forecasts that the growth rate will recover to 0.49% in 2017, 1.43% in 2018, 1.72% in 2019 and 2.04% in 2020 this growth is simply not enough. The slowdown in GDP growth also has a negative impact on unemployment rates in the country.

The unemployment rate statistics continue to be a big concern for the South African government. According to Statistics South Africa (StatsSA, 2016) in the first quarter of 2016 unemployment rates in South Africa are reported to be 26.7%, compared to 26.4% in the first quarter of 2015, equating to a 0.3% increase in unemployment. The Seed Academy estimates that almost half of the unemployed are below the age of 35, otherwise classified as “youth” in South Africa. As franchises are “proven” business models and youth lacking the necessary business experience could benefit from entering the business world via a franchise.

Government, through the 2016 Budget Review has acknowledged that in order to “meet its ambitious national development targets, South Africa needs a far higher rate of inclusive, job-creating economic growth.” With the economic growth and unemployment statistics not looking promising, the South African government is encouraging entrepreneurship as way to reduce unemployment and poverty. The Budget Review also lists key areas of intervention to increase economic growth rates in the medium- and long-term. Included in these intended areas are the following (National Treasury Budget Review, 2016):

- Stimulating economic activity. Public institutions with strong balance sheets, including development finance institutions and social security funds, will make greater use of their resources to back economic stimulus and job creation.
- Encouraging the growth of small business. The National Treasury and the Department of Small Business Development are working with the private sector to explore establishing a small business innovation fund.

The SME (sometimes referred to as the SMME) sector in South Africa is a key stakeholder in job creation and the interventions from government as proposed above show that government also recognises this. There are various definitions of SMMEs, dependent on sector, size and jurisdiction. In South Africa, the most widely used definition is according to the DTI, which uses turnover thresholds to establish the classification of a business.

In Table 1 below are the September 2018 thresholds according to the DTI, adjusted for inflation by StatsSA .

Table 1: DTI's cut-off points (adjusted by StatsSA) for Quarterly Financial Statistics

Industry turnover	Large > Rm	Medium> Rm	Small> Rm	Micro> Rm
SIC2 Mining and quarrying	526.5	135.0	54.0	2.0
SIC3 Manufacturing	688.5	175.5	67.5	2.0
SIC4 Electricity, gas and water supply	688.5	175.5	68.8	2.0
SIC5 Construction	351.0	81.0	40.5	2.0
SIC61 Wholesale trade	864.0	432.0	81.0	2.0
SIC62 Retail trade	526.5	256.5	54.0	2.0
SIC63 Motor trade	526.5	256.5	54.0	2.0
SIC64 Accommodation and catering	175.5	81.0	68.5	2.0
SIC7 Transport, storage and communication	351.0	175.5	40.5	2.0
SIC8 Real estate and other business services, excluding financial intermediation and insurance	351.0	175.5	40.5	2.0
SIC9 Community, social and personal services, excluding government and educational institutions	175.5	81.0	13.5	2.0

In her research on franchisees, Constantaras (2017) states that of the 300 franchisees that partook in the research, the median annual turnover is R2, 680,000. Though the median turnover is R 2 680 000, it can be seen in Appendix C: Figure 5 that the range of the turnover is wide. In 2017 11 of the 300 participants had a turnover of below R250 000, in the same year 11 of the 300 participants had a turnover above R20 million.

1.1.1 Criteria required in order to qualify as a franchisee or to own a franchise

Franchisors have over the years used different criteria in selecting a suitable franchisee to partner with. Tatham, Douglas, and Bush (1972) found that, once the franchisor has made the decision to franchise, finding a suitable franchisee is one of the single most operative issues the franchisor faced. Some of the criteria is qualitative and some quantitative. The qualitative criteria would be factors such as personality and attitude.

Just as franchisees find it challenging to enter the franchise sector, franchisors do also face challenges. Gikonyo, Berndt, and Wadawi (2015) did a study on critical success factors (CSF) for franchised restaurants in Kenya. Amongst the CSF listed was the selection of excellent franchisees.

One of the main challenges for franchisors is selecting the “right” franchisees to partner with. There are various important criteria that can be used to assist franchisors select the best possible franchisees. Although there is a lot of literature on selecting the best franchisees, there are some common themes in what constitutes a good franchisee candidate.

Some of the key criteria are listed in Table 2 below:

Table 2: Criteria to qualify as a franchisee

Criteria	
Brand Champion	Though Walker (2016) focuses on the selection criteria for international franchisees, he highlights the importance of ensuring that potential franchisees are passionate about the brand they are buying into., this would be applicable to all franchisees whether local or international. Norwell (2010) also suggests that a franchisor should choose franchisees that have the same core values and are engaged with their business.
Communication	Ensuring that the franchisee’s expectations are realistic and managed is a key CFS according to Gikonyo et al. (2015). It is thus important to ensure that a franchisee is a good communicator, not only to be able to “sell” the brand but to also be a good listener to receive the necessary guidance from the franchisor.
Corporate culture alignment	Walker (2016) emphasises the importance of having corporate cultural alignment between franchisor and franchisee. Ensuring that a prospective franchisees corporate culture aligns with that of the franchisor will reduce the chance of future disputes.
Alignment of goals and strategies	Franchisors and franchisees need to review their respective business plans and ensure that their goals and strategic outlooks for the business are aligned.
Market expert	The franchisee should have good knowledge of the market the franchise operates in.
Realistic expectations	ABSA Franchising (2015) suggests that franchisors and franchisees draft letters detailing their legitimate expectations and these letters be

	discussed prior to the two parties entering into a franchise agreement. This ensures that both parties are aligned with regard to expectations from the relationship and that unrealistic expectations are discussed and eliminated from the onset.
Access to resources	Running a franchise require various resources besides financial resources. These resources human resources, access to location, access to site utilities such as power and water and other logistics.
Financial strength	Ensuring that candidate is aware of and capable of meeting all financial obligations, current and future is an important criterion that franchisors should investigate, according to Walker (2016).

1.2 Problem statement

Raising finance is a key barrier to entry for most SMMEs as proven by numerous studies. Mutoko and Kapunda (2017) found that the number one challenge for SMMEs in Botswana, particularly SMMEs in manufacturing was lack of finance. Mutoko and Kapunda (2017) also state that a bank’s decision on whether to finance a lender is influenced by numerous factors such as age, gender, experience, credit history or if the lender is an enterprise the decision to lend is influenced by business experience, turnover and earnings, amongst others. Haron (2013) also cites lack of finance amongst the challenges facing SMMEs.

As seen in Appendix C: Figure 3 (pg. 68), entrepreneurs that took part in the 2016 questionnaire for start-ups listed the inability to raise funds as the second biggest challenge they face. In addition to this, the questionnaire also shows that 85% of participants self-funded their start-up ventures- see Appendix C: Figure 4.

Finance is a broad term that has numerous definitions dependent on the context in which it is used. Kurt (2019) defines *finance* as “broad term that describes two related activities: the study of how money is managed and the actual process of acquiring needed funds”. The Cambridge Dictionary (n.d.) defines finance as “(verb) to provide the money needed for something to happen”. For the purposes of this paper, the definition of finance that is applicable is the process of acquiring needed funds.

In her policy insights titled “Financing SMEs in Africa”, Kauffmann (2005) notes that Africa’s SMEs have little access to formal finance, resulting in SMEs struggling to start up and/or grow. Formal finance can be defined as funding obtained from formal sources.

Finance or credit can be sourced from two broad categories i.e. formal sources and informal sources. Formal sources are institutions that are regulated by government such as banks and cooperatives.

The lack of access to “formal” finance means that SMEs are financed via informal means such as personal savings or retained earnings. In his report on financing SMEs in Africa, Quartey (2007) notes that many SMEs in Africa, particularly in Nigeria and Ghana have financed their businesses using other informal sources such as owner’s savings, money lenders, friends and relatives, credit and savings associations and susu.

In order to fully understand this challenge, one would need to analyse what is meant by funding and with the amount of seemingly available capital in the market why is it that entrepreneurs are unable to access it.

Kauffmann (2005) outlines numerous reasons why SMEs are unable to access finance. These being the high risk of default amongst SMEs, the SMEs inability to meet conditions set out by financial institutions, poor guarantees or collateral from SMEs and a lack of information about SMEs and their ability to repay the loans they seek.

Interestingly, Kauffmann (2005) continues on to suggest ways on how SMEs can be assisted to meet the requirements of formal financiers. Kauffmann suggests the following financial instruments to be used:

- Franchising: in order to address the problem of lack of information about SMEs and their ability to repay the loans they seek.
This is because the brand name of the franchise is known and the benefit of being able to use the know-how of the franchisor reduces the risk of failure
- Guarantees on loans: these guarantees would be from a party that has a strong balance sheet to be able to step into the shoes of the lender should he/she be unable to fulfil their debt/loan repayment obligations
- Leasing and factoring: although these instruments can reduce risk, they are not used a lot in Africa.

The Seed Academy (2016) (Appendix C: Figure 4) also noted that entrepreneurs find that despite the support there is in the market, there is a gap when it came to early stage funding. This means

that even with funding being available from institutions such as DFIs, entrepreneurs still struggle to access these funds, with only 2% having received funding from DFIs and /or financial institutions.

As seen in Appendix C: Figure 3, on page 70 of this study, entrepreneurs that took part in the 2016 questionnaire for start-ups listed the inability to raise funds as the second biggest challenge they face. In addition to this the questionnaire also shows that 85% of the participants self-funded their start-up ventures – see Appendix C: Figure 4 (page 70 of this study). With government and the private sector so keen to finance start-ups, the challenge remains that 85% are self-funded.

Entrepreneurs often have great difficulty in raising owner's contributions. The attempt to raise this capital often has negative consequences on their personal financial position, their families and lifestyle. With so much expected of the entrepreneur, the question remains; how accessible is funding?

1.2.1 Franchisee's owners' equity requirement

When applying for finance at most institutions, prospective franchisees are required to also contribute to the total funding required; this is known as owner's contribution or unencumbered funds (Olufisayo, 2011)). The levels required by franchisors can be up to 50% of the cost of the franchise. Often, this requirement makes it difficult for entrepreneurs to meet the requirements of a prospective funder. As an example, assuming a franchisee would like to purchase a franchise valued at R1 million. A potential funder may require that 50% of this be owner's contribution. In this instance a franchisee would need to raise R500 000 to access a loan of R500 000 from a debt financier.

How does the entrepreneur then raise this R500 000? What challenges do they experience in trying to raise owners' contribution? What are the effects of this on their standard of living and business model? How did the entrepreneurs in this study overcome these challenges? What lessons did they learn in the process of raising owner's contribution do they think will be useful to prospective franchisees?

Lewis (2009) lists one of the disadvantages of acquiring a franchise as opposed to an independent business as the cost element, further expanding on this by explaining that buying into a well-known franchise is expensive.

As evidenced by the studies referenced in preceding paragraphs, access to funding remains a big challenge for SMMEs and entrepreneurs. In order to access corporate finance in the form of loans for example, entrepreneurs are expected to contribute equity to the business venture. There is however limited literature on how entrepreneurs financed the equity contributions required by financial institutions. The literature is even more limited on franchisees. Furthermore, once franchisees have raised unencumbered equity, this study aims to explore/examine how franchisees financed their owner's contribution and examine the challenges franchisees faced in raising this capital.

1.3 The aim and objectives of the study

The aim of this study was to establish what avenues are available for franchisees to raise owner's contribution when purchasing a franchise.

The research sought to:

1. Examine how much franchisees paid to purchase their first franchise and what portion of it was required to be raised as owners' equity. The research further sought to examine how the franchisees they raised this requirement.
2. Identify what challenges franchisees experienced in raising the owner's contribution requirement.
3. Assess what impact these challenges had on the franchisees, their finances, their business and/or their family and friends.

1.4 Research questions and scope

Based on the preceding readings and background as well as the literature included in the literature review to follow, the research sought to answer the following questions:

- 1.4.1 What is the average owner's contribution that franchisees are required to make in order to purchase a franchise and how did the franchisee raise this requirement?
- 1.4.2 What challenges did the franchisees face in raising the required owner's contribution?
- 1.4.3 What impact did the raising of the owner's contribution have on the franchisees, their finances, their business and/or their family and friends?

1.5 Purpose and significance of the research

The purpose of this study is to investigate how franchisees have financed their owner's contribution when purchasing a franchise. The study also sought to establish what impact the chosen source of funding had on the franchisee and their aspirations, both personal and business.

This was done by studying existing literature on small business finance, through an online franchisee survey, conducting interviews with potential financiers as well as franchisors.

There is substantial research on SMMEs and entrepreneurship. There is however negligible research on how franchisees finance their equity or owner's contribution. This study seeks to provide additional insight into this. The study will be of benefit to business/commerce students, financiers, financial advisors and consultants as well as aspiring entrepreneurs.

Commerce students will benefit from the study as it will provide additional information that is not currently available on franchising and entrepreneurship, with which they will be able to deepen their understanding of the academic course they have chosen.

Financiers and advisors will get insight on the challenges that faces franchisees and as a result could investigate innovative financial solutions tailor made for franchisees.

From studying the challenges of those that came before them prospective entrepreneurs will get the benefit of learning from past mistakes, replicating what has worked well and possibly improving on the methods of their predecessors to achieve an even better outcome when it comes to financing their businesses.

1.6 Conclusion and overview of chapters

This chapter of this research illustrates that indeed franchises carry some great advantages for South Africa and its economy. The financing of potential franchisees however remains a problem that requires creative solutions to solve. Studying existing franchisees and how they financed their franchises could assist in cultivating some of these solutions.

Chapter Two of this study provides a brief analysis of the literature that currently exists on SMME finance, with a focus on franchise finance in South Africa and Africa at large. In Chapter Three, the research methodologies adopted in this dissertation are unpacked to examine the challenges faced by franchisees in raising owner's contribution. Chapter Four is a summary of the research findings. In Chapter Five, the conclusions of the research are outlined and lastly, Chapter Six

provides some recommendations on areas that future research papers could focus on to expand on the findings of this paper.

CHAPTER TWO: LITERATURE REVIEW

2.1 Introduction

This chapter of the study aims to briefly outline the theoretical foundation(s) of franchises, to analyse and review key empirical literature that exists on franchises as well as to provide an overview of the franchise industry in South Africa.

2.2 Background on franchises

According to Illetschko (2005), franchising originates from the United States of America and dates as far back as the 1860's. Mr. Isaac Singer is given credit as being the man to start a modern-day model of franchising when he wanted to distribute his sewing machine products to a wider consumer base but lacked the funding to increase production. Also, his customers required training to use the machines which is retailers were not able to provide.

Mr. Singer then decided to sell licenses to people giving them the right to sell his machines in certain geographical areas, with them being responsible for the training of the consumer on the usage of the product. This became a win-win solution in that Mr. Singer used the proceeds from the sale of licenses to increase production and the holders of the licenses received access to sell an established brand.

In 1954, Ray Kroc – a milkshake mixer salesman discovered a hamburger stand owned by two brothers. He discovered the reason they were buying so many of his mixers was because of the success of their high-volume production system. They were able to provide their customers with fast service at low cost. Mr. Kroc became their license agent and started to sell their franchise all over the USA, starting in Chicago. He later bought out the Mc Donald's brother stake. Today Mc Donald has over 36 000 restaurants worldwide.

Even though various countries via license agreements with the USA went on to open franchises of USA brands in their countries, South Africa had to develop their own brands and systems as a result of the trade embargos that were imposed on it pre –democracy. Prior to unpacking franchising in South Africa, it is useful to first define what franchising is.

2.3 Franchising defined

There are various definitions and interpretations of the concept of a franchise. Some of these being:

- Franchising: “A franchise industry is one where an entrepreneur can purchase the right to set up a branch of an established industry (service or manufacturing). The franchiser maintains a degree of control to ensure uniform standards of quality and the franchisee can benefit from marketing a known and established product. Franchising is a growth area in South Africa” (Macleod, 1999).
- Franchising: “The business format franchise relationship is characterised by a continuing business relationship between the franchisor and the franchisee that extends beyond the implications of the product or service and trademark. It encompasses the entire business process, including marketing and advertising strategies, operating standards and procedures, accounting practices, quality control and operational standards. Above all, close communications between franchisor and franchisee will be maintained on an ongoing basis” (Illetschko, 2002).

The definition of a franchise that prevails in this paper, as adopted by FASA, is as follows; “A *franchise* is a grant by the franchisor to the franchisee, entitling the latter to the use of a complete business package containing all the elements necessary to establish a previously untrained person in the franchised business and enable him/her to operate it on an ongoing basis, according to guidelines supplied, efficiently and profitably” (FASA Franchising Q&A, 2018)

2.4 Overview of the franchise industry in South Africa

The trade embargoes imposed on South Africa worked to South Africa’s advantage. As a result of not having access to the USA brand licenses, South African entrepreneurs had to be innovative and come up with their own brands and concepts. Franchise Direct (2011) provided a brief history of franchises in South Africa from the 1960’s when Mr. George Halamandaris started the Steers franchise after taking a holiday in the United States. In the 1970’s an iconic brand in South Africa was born, this being Shoprite which opened its first store in Cape Town in 1979. In 1982 Chicken Licken, a fried chicken fast-food chain was opened in Johannesburg. Today there are over 200 Chicken Licken stores in more than four African countries. Another popular chicken brand that was born in the 80’s is Nando’s. Other franchise concepts continued to be opened after this. In 1991, Debonairs, a pizza chain was started by Craig McKenzie and another university student.

Franchising continues to grow rapidly in South Africa, with most franchises operating in South Africa being locally developed and founded.

In a questionnaire conducted by NAMAC Trust (which is now a division with SEDA), with some results summarised in Appendix B: Table 1, it was observed that in 2004 there were a total of 391 franchise concepts operating in South Africa, of which 90.5% were local concepts (FRAIN, 2004). In the same period the franchise sector generated an estimated R129.1 billion in revenue and employed an estimated 284 000 people. Franchising made a 17.1% contribution to the GDP.

Fast forward to 2015, these statistics continued to grow. According to a survey carried out by FASA in May 2015, there were over 690 franchise concepts in South Africa. This is an estimated 60% increase in the 11-year period from 2004 to 2015. The estimated revenue generated was R465 billion and number of employees an estimated 329 245. The revenue generated has increased by 260% and the number of employees by 16% from 2004 to 2015. Franchising is currently credited for contributing over 12% to the GDP of South Africa.

In the most recent survey conducted by FASA in 2017, South Africa was found to have over 845 franchised systems with over 40 528 stores. The total value of the franchise industry amounts to R587 billion or a contribution of 13.3% to the GDP.

2.5 Why entrepreneurs choose franchising

Macleod (1999) states that opening a franchise is one of the best opportunities for aspiring entrepreneurs. He lists various advantages for going the franchise route and concludes that in the end, the advantages of opening a franchise far outweigh the disadvantages. Some of the advantages he notes are:

- i. Possible discounts on input costs because of the franchisor purchasing in bulk
- ii. Benefiting from an established product and brand
- iii. Training and ongoing advice from franchisor
- iv. Easier access to loan capital because of the reduced business risk

When Constantaras (2017) conducted her research on franchisees, one of the questions she asked was how long the franchisees first franchise that partook in her research had been in operation. The results were as follows:

- Two years and under – 11%
- Two to five years – 20%
- Five to ten years – 28% and
- Ten years plus – 41%

It is not disputed that opening a franchise can present immense opportunities for entrepreneurs if utilised correctly. Entrepreneurs however have a lot of challenges facing them, particularly as start-ups. Entrepreneurs across the board list access to funding as a key barrier. It is therefore important to assess the extent the lack of access to capital impacts the growth of entrepreneurs or growth of the franchise business sector.

Before going into the details of how franchisees can source funding, the next paragraph looks at the cost of franchises in South Africa.

2.6 Definition of a successful franchisee and key franchisee attributes

Nathan (2006) defines a successful franchisee as someone that maximises the profit potential of their business, ensures all customers have a great experience every time and is comfortable adopting the role of franchisee.

Without going into too much detail on the above, Nathan (2006) further states that, in order to ensure that a franchisor selects a franchisee that has a high chance of success, the franchisor must ensure that the franchisee has some key attributes that will contribute to their success. These attributes include but are not limited to the franchisee having adequate reserves of working capital should the business be slower to grow than anticipated, the franchisee should have an interest in finance and business affairs, have the emotional support of friends and family but still be able to work independently. The franchisee should be able to get things done efficiently, be well organised and proud of one's personal presentation. The franchisee should possess both physical and emotional resilience and be comfortable selling to people. To increase their odds of success franchisees should be able to organise and motivate others to get things done and be team players. Franchisees should be trustworthy in giving accurate information, particularly to franchisors and have a realistic understanding of the franchise relationship and the obligations of both parties.

Most of the literature on franchisor selection criteria for a franchise emphasise the requirement that potential franchisees must have the necessary capital to not only purchase a franchise (start-up costs) but to also operate the franchise going forward (working capital). Whilst the financial

capability of franchisees is one of the critical components in the selection process, notes Walker (2016), franchisors should note that this is just one element of the selection process. Unfortunately, far too often franchisees are selected on this metric exclusively.

Even though the financial capacity of franchisees is not the only selection criteria, it is certainly important.

2.7 Cost of franchises in South Africa

The cost of purchasing a franchise in South Africa varies from sector to sector. According to FRAIN (2004) and as can be seen in Table 3 below, franchise concepts can be broken down into various industry sectors. Some of these industry sectors are listed below:

Table 3: Franchise industry sectors

Industry Sectors
Automotive products and services
Building and home maintenance
Business to business supplies
Education and training
Fast food/take out
Health and beauty services
Other business sectors
Real estate agencies
Restaurants/sit down
Retail incl. convenience stores
Video rental and entertainment
Petrol supplies

One of the disadvantages of penetrating the world of business by purchasing a franchise is that some franchises are expensive (Macleod, 1999). There are several things that influence the cost of a franchise. These being the size, sector and location, amongst others.

In 2015 a fast food restaurant could cost anything from R499 000 to R6 000 000 according to BusinessTech. A Chesa Nyama would set a franchisee R499 000 whilst at the higher end of the

scale a McDonalds would cost R6 000 000. A franchise fee which is at times charged in addition to the acquisition cost is not included in the above start-up costs. These franchise fees can be anything from R54 000 to R540 000.

A Pick n Pay store would cost a franchisee an estimated R9 512 000. These costs will also vary depending on size and location of the store.

In Appendix B: Table 3, Sorbet, a health and beauty spa with over 150 stores in South Africa sets out their start-up costs for potential franchisees. These costs vary from an estimated total of R816 000 to R1 600 000.

A BP service station can cost anything from R3 000 000 to R13 000 000.

Depending on the franchise purchased, the cost can be as low as R50 000 but can go up R13 000 000 and even beyond depending on the factors listed prior.

In addition, an article written by Which Franchise (“Common financial mistakes made by new franchisees”, 2016) states lack of funds as a key cause of failure for franchises. It goes on to say that franchisees, often underestimate the operational costs of owning a franchise, which are cost above and beyond the initial upfront fee to purchase the franchise. A franchisee can expect that the franchise will lose money for the first two years, losses that will need to be carried by the franchisee(s) until the franchise breaks even and eventually starts making money. The franchisee thus requires a financial cushion to be able to contend with unexpected challenges of running a business. The article further states ten (10) common mistakes made by franchisees, unsurprisingly seven out of the ten mistakes are financial, concluding that franchisees often underestimate the costs of owning a franchise, often only focusing on the initial purchase price.

2.8 Source of finance for a start-up franchise

Once a franchisee has established which franchise they would like to purchase and how much they will require to purchase and start-up a franchise; the next question they will need to answer is how they will finance this requirement. Capital consists out of two broad structures, debt and equity.

Debt financing

Chen (2019) defines debt as *an amount of money borrowed by one party from another. Debt is used by many corporations and individuals as a method of making large purchases that they could not afford under normal circumstances. A debt arrangement gives the borrowing party permission to borrow money under the condition that it is to be paid back at a later date, usually with interest.*

Equity's definition depends very much on the context. *In finance in general, you can think of equity as one's ownership in any asset after all debts associated with that asset are paid off. For example, a car or house with no outstanding debt is considered entirely the owner's equity because he or she can readily sell the item for cash, with no debt standing between the owner and the sale.*

ABSA Franchising also defines equity as *the amount of money you (and your business partners if applicable) plan to contribute from own unencumbered sources.*

Which Franchise ((2017) states that there is no shortage of funds for start-ups but rather a shortage of entrepreneurs that are willing and able to present financiers with a well thought out business proposal, otherwise known as a business plan, with owners contribution and security forming an integral part of this business proposal.

According to Hisrich and Peters (1998), a business plan is the single most important document when applying for funding for a start-up.

A franchisee can approach various lenders for their start-up funding. These being banks, development finance institutions and other private sector financial institutions.

In his article, Larson (2012) notes that often SMEs are too big for microfinance but too "small" for banks that want to invest in small businesses but are unable to because of a lack of information and the unknown risk. The challenges of access to finance for entrepreneurs increase substantially for black entrepreneurs. Zama (2017) notes that even with apartheid being abolished in 1994, black entrepreneurs still struggle with access to affordable credit. He further asserts that although South Africa (SA) boasts one of the most sophisticated financial systems on the African continent, but even so still suffers from challenges related to financial inclusion of formerly marginalised entrepreneurs such as women and entry level black entrepreneurs.

According to Illetschko (2002), private banks have various financial products specifically to finance small business. Most commercial banks also have specialised franchise divisions that deal specifically with franchise transactions. It is evident that the private sector as well as public finance institutions have a healthy appetite to loan franchisees capital. Illetschko (2002) notes that banks love franchise transactions, mainly because the business risk is reduced when investing in a franchise. And because the franchisor also shares in the risk; should the franchisee fail, it will have a negative impact on the franchisor and they will lose out on ongoing management fees they have a vested interest in ensuring that franchisee gets all the support they require.

Equity financing

Even with all this, financiers will still expect that an entrepreneur invests some of their own money in the venture for the following reasons:

- Having accumulated capital demonstrates that the applicant can handle money and financial affairs responsibly
- It shows that you are committed and will continue to be committed to the venture as you have put your own money at stake
- The debt funding will attract interest, in the absence of equity the cash flows of the business might be insufficient to service the loans and thus put the business in jeopardy

Research conducted by Pretorius and Shaw (2004) concluded that, although a good business ABSA Franchising (2015) also goes on to state that most prospective franchisees “become unstuck” when it comes to the equity or owner’s contribution that they must make towards the purchase of a franchise. Even with this observation, the ABSA Franchising does not provide suggestions into where they propose entrepreneurs get this owners’ equity.

In 2001 a task group of the Policy Board for Financial Service and Regulation concluded their review of the funding of Small to Medium Enterprises (SMEs) in South Africa. One of the areas that their report covered was the access that SMEs had to equity and debt capital. In their study the task team noted that small businesses often do not meet the criteria to obtain debt funding. One of the key observations in this paper was that whilst there are a lot of debt products available for SMEs, little attention is being given to equity finance products.

In March 2000, Don Cruickshank completed a two-year review on competition in UK banking Services (the “Review”). Cruickshank found that there was a market failure in the provision of equity finance to SMEs. He concluded that this failure was even more significant than access to debt failures. His key recommendations were that venture capital funds needed to be established and/or supported so that these could fill the market failures observed in the provision of equity finance for SMEs.

In noting the recommendations made by Cruickshank (2000), the task group noted that South Africa faces similar challenges as the UK when it came to equity financing of SMEs. The task group listed some key advantages and disadvantages of equity financing. The advantages identified were that dividends are only paid on profits and only to the extent that the company’s shareholders

decide to distribute dividends, implying that the enterprise is not impairing its cash flow during the initial 'take-off' phase or during cyclical 'downs'. The payment of dividends therefore has more flexibility than debt where the interest and capital on the loan must be paid to financiers regardless of how the enterprises financial performance is. The holders of equity are business partners who not only help with funding aspects, but also with financial, corporate governance and management issues in a broader sense. The equity capital submitted by shareholders is long-term funding that need not be repaid. It can be repaid, though, in the form of dividends or share buybacks. The 'cushion' provided by equity capital augments the firm's ability to contract debt, i.e. it can be leveraged.

Though equity does have some advantages, the disadvantage identified by the task group are that issuing of equity results in a dilution of the initial owner's business interests, meaning a smaller share of profits and a smaller percentage of the voting rights for important decisions. Also, shareholders may demand greater disclosure than the owner is willing to make (often for competitive reasons). Shareholders may start to interfere in the day-to-day activities of the company. Unlike interest, dividends are not deductible from tax and thus the tax bill for the entity will be higher. If the business is successful, it might be difficult to buy back the shares of other shareholders or to launch a general share-buyback scheme should the entrepreneur wish.

The bulk of South African franchises can be classified as SMEs. Franchises should then not be exempt from the challenges facing other SMEs. If this is the case, where then do financiers expect the equity contribution from franchisees to come from? And are there any advantages for financiers to financing equity in SMEs? If advantages indeed exist, why is it that financiers are not capitalising?

The task group goes further and suggests a possible advantage for financiers to fund equity in SMEs, that being the high-risk high reward principle. Equity investors can reap the rewards of being long term investors and partake in the upside should the venture succeed.

This being the case, why then are financiers still reluctant to finance via equity in SMEs? Cruickshank lists transaction costs being the main deterrent for venture capital firms to finance in the SME sector. The transaction costs of venture capital firms are simply too high to make the funds worthwhile.

2.9 Capital structure theories

Elomo (2014) describes capital structure as the proportion of debt and equity used by a firm to finance its operations.

There are three main theories that are recognised by Sogorb-Mira (2002) as relevant for the determination of the capital structure of SMEs. These theories are:

2.9.1 Trade off theory

This theory suggests that a firm will use debt if the tax shields of debt outweigh the cost of potential financial distress. This means that in considering an optimal capital structure taxation and the possibility of bankruptcy must be considered. Debt usually has tax benefits. The more debt a firm has the higher these benefits. However, the more debt a firm has the higher the chances of not being able to service this debt and thus being declared bankrupt. This is the trade-off between tax and bankruptcy.

2.9.2 Agency theory

According to this theory in instances where firms want their management to use funds more efficiently, they use more debt to finance the firm. This theory concludes that management will be less careful in decision making when the funds come from the shareholders. When the funds to finance projects comes from lenders that require that it be paid back, managers tend to use it efficiently. SMEs do not often experience agency problems that arise between shareholders and management as in most cases with start-up SMEs, the owners are usefully the managers as well.

2.9.3 Pecking order theory

Myers and Majluf (1984) suggest that when looking to finance ventures, firms follow the following pecking order; they first finance using internal funds, then low-cost debt then finally and when all else has failed, equity.

With start-ups the option of using internally generated funds will not be available as the business has not started operating. This means under this theory an entrepreneur will finance the business using debt in as far as possible and when they have exhausted all debt options will inject equity.

According to Jensen and Meckling (1976), the optimal capitals structure is achieved by trading off the agency costs of debt against the benefits that the entity would derive from debt. The optimal capital structure will differ from business to business and is influenced by various factors. These

factors include the age of the firm, size of firm, asset structure, profitability, growth and firm risk, managerial competencies, business information, networking and location.

These factors are explained in Table 4.

Table 4: Optimal capital structure influencer

Optimal capital structure influencer	Description
Age of firm	Older firms access finance easier than younger firms. This is because older firms would have built up a reputation and financial track record. Older firms also have cash flow that have been generated which new firms do not have. A start-up franchisee will as such find it harder to access debt funding than existing franchisees with a track record.
Size of firm	Larger firms are seen to be more robust and diverse. As such larger firms have easier access to finance than smaller firms. Franchise start-ups usually start small, in one location.
Asset structure	A firm that has more tangible and liquid assets will have higher collateral and thus can access debt funding easier than a firm with no asset base.
Profitability and growth	The pecking order assumes a negative relationship between profitability and debt financing i.e. the higher the profitability the lower the debt levels as the company will use its internal profits to finance growth. The trade-off theory however assumes a positive relationship between profitability and debt financing.
Firm risk	Business risk is negatively related to debt finance. The higher the perceived business risk, the lower the chances of accessing debt finance.
Managerial competencies	Educational and other competencies increase the chances of accessing debt finance as these have a positive impact on the start-up's performance.
Business information	In a new venture, the business plan will provide the financial information required to assess the debt application. This information therefore needs to reflect the businesses ability to service debt.

Networking	Relationships created via networking can build legitimacy and credibility. Working on relationships with financiers and creditors will make the process of applying for finance easier as they will now be familiar with an entrepreneur and their track record.
Location	Firms located in metropolitan areas have a higher success rate than those located in rural areas. These firms in metropolitan areas will as such have better access to finance than those in rural areas.

2.10 Optimal capital structure for a start-up franchise

As a result of the many influences on a firm's capital structure it is not possible to have a blanket capital structure for all categories of start-up firms. All the factors that influence the capital structure will have to be assessed and a bespoke capital structure derived for each business. This is true in the case of franchises. Although no uniform capital structure exists for franchises across all the sectors that they operate, there is always a need for the potential franchisee to contribute equity when approaching a lender for funding.

Additionally, most franchisors list owner's contribution as a requirement prior to a potential franchisee being approved. The percentage owner's contribution/equity required varies from franchisor to franchisor.

According to Which Franchise, the actual amount varies depending on the borrower's risk profile, the standing of the brand and the business's cash flow projections but as a rough guide, a bank will lend 30-50% of the required total. This means that the balance of 70- 50% will be financed with equity. Which Franchise also goes on to state that franchisees often make the mistake of over-leveraging their franchise i.e. the debt level being higher than the equity. This suggests that in determining a capital structure for one's franchise, a franchisee should not have the debt levels being above 50%.

2.11 Sources of owners' equity

In the 2016 questionnaire carried out by Seed Academy on start-ups, 85% of participants had financed their start-ups using their own resources. 9% had received funding from friends and family and 2% from angel investors.

Compared to the same questionnaire conducted in 2015, the participants that funded their start-ups from own resources increased by 2% from 83% in 2015. Those that received finance from friends and family also increased by 2% from 7% in 2015. The angel investors remained the same at 2%.

2.11.1 Own resources or savings

Entrepreneurs predominantly finance their start-ups from their **own resources**. These resources are usually from sources such as retirement savings, retrenchment packages, normal savings, sales of assets and re-mortgages. There are advantages to using your own resources to finance your business.

Amongst these is that it is less risky to finance using your own funds as external investors will seek to maximise their value which might be to the entrepreneur's disadvantage. Another advantage is that the entrepreneur will have more control and flexibility over how to spend their resources. When borrowing externally financiers can put restrictions on what the money can be used for as well as restrictions on the operations of the firm.

2.11.2 Angel investors

Angel investors are people or companies that buy equity in small firms. Investopedia defines angel investors as *investors that invest in small start-ups or entrepreneurs. Often, angel investors are among an entrepreneur's family and friends. The capital angel investors provide may be a one-time investment to help the business propel or an ongoing injection of money to support and carry the company through its difficult early stages.*

Angel investors are few and far between and are therefore difficult to find.

It is unclear from current literature how many start-up franchises in South Africa were financed by angel investors, if any. This could be an area where additional studies could be carried out, to ascertain the prevalence of angel investors in South Africa and how many of these have an appetite to invest in franchises.

2.11.3 Friends and family

Friends and family can also offer what is referred to as soft loans. This means that the terms of their funding are not that strict, interest is minimal or not charged at all. Usually there is no expectation that this money invested will be returned. Receiving start-up funding from friends and family may have some drawbacks though, such as friends and family wanting discounted or free

goods and services from you. If expectations are not managed resulting tensions may also affect relationships negatively.

The surveys conducted by Seed Academy do not distinguish franchises, they were carried out on start-up SMMEs a whole. It would be useful to see if these statistics differ when franchises are isolated.

2.12 Commitment levels

A lot of literature concludes that one of the reasons for requiring a shareholder's contribution is to ascertain how committed the entrepreneur is to the venture. The common belief, being, the more money an entrepreneur has contributed from their own pocket the more committed they will be to make the business work.

The inverse of this is that with little money invested in the business entrepreneurs will have little incentive to working hard for the business to succeed.

Standard Bank (2005), in their Practical Guide to Business Owners also notes that financiers are more likely to give an entrepreneur a loan if they have already invested some of their own money into the business as this demonstrates commitment and confidence.

Nafu Farmer (2008) states that banks are reluctant to grant loans to first time farmers (or any entrepreneur for that matter). For this reason, it is important to note that in order to increase your chances of getting a loan approval you should be willing to invest your own cash.

2.13 Conclusion

In conclusion, franchises in South Africa continue to contribute to South Africa's economy and employment figures. As such, in an endeavour to boost South Africa's economic growth and promote entrepreneurship, government and all relevant stakeholders should continue support this important business sector. Access to finance remains a challenge for franchisees, with owner contribution requirements being an obstacle for a lot of franchisees. The remainder of this study looks at how franchisees financed their owners' contributions for the purchase of their first franchise. It further looks at the impact the chosen source of owner's contribution had on franchisees, their businesses, and relations.

An online survey was used to gather data from franchisees.

CHAPTER THREE: RESEARCH METHODOLOGY

3. Introduction

This chapter of the research paper outlines the approach and strategy adapted to explore how the franchisees that partook in the research financed the owner's equity required when purchasing a franchise. The research methodologies used to gather data is explained as well as the reasons why these methods are deemed appropriate. The rest of the chapter goes on to explain how, when and how often data was collected. Finally, it describes the methods used to analyse the data, how reliable these methods are and considers some of the limitations of the research method used.

3.1 Research approach and strategy

To answer the research questions as outlined in Chapter One of this paper, it was important to investigate what research methodology would be most suitable to maximise the validity and reliability of results. In conducting any study, there are three main approaches that can be utilised, namely a qualitative approach, quantitative approach or mixed approach, which is an approach that combines or integrates both qualitative and quantitative methods, according to Creswell and Clark (2011).

The research approach and strategy adopted for this study was an exploratory and inductive one, using the qualitative approach to collect and analyse data to arrive at the conclusions reached and recommendations made.

3.1.1 Qualitative research

The qualitative approach is a naturalistic method that seeks to understand phenomena in context specific settings where the researcher does not manipulate the phenomena of interest (Patton, 2002). The qualitative approach is used to address "how" questions rather than "how many" to understand the life experiences and perspectives of those being studied (Lee, 2014).

Although this study is a qualitative study, some quantitative information was also collected from participants. The main reason for collecting some quantitative data from participants for this study is to contextualise and support the qualitative research and to provide further insight and understanding of the challenges (qualitative) that franchisees face in raising finance, thus

enhancing the interpretation of the results. This research paper seeks to explore “*how*” franchisees financed the purchase of their first franchise and the challenges (if any) they faced.

In the absence of some quantitative data it would be challenging for the researcher to contextualise and comprehend the results of the qualitative data collected. Although this study does collect limited quantitative data from participants, this is done to contextualise the research questions. An example of the quantitative data collected is the average amount that participants had to raise. Without the quantitative data it would be difficult to appreciate the materiality of the amount and why it would be a challenge to raise for some participants.

The remainder of the questions in the questionnaire and those at the crux of this study were qualitative questions.

3.2 Research design

Qualitative research designs are flexible rather than fixed (Robin, 2011) and inductive as opposed to following a strict sequence or being derived from a decision or hypothesis made at the onset. There are a variety of qualitative research designs or strategies, Merriam (2002) states that the most used are: basic interpretive, phenomenology, grounded theory, case study, ethnography, narrative analysis, critical and postmodern-post-structural.

This study the basic interpretive strategy was used as the researcher sought to understand the perspectives, experiences and worldwide views of the participants.

3.3 Data collection

Merriam (2002) further suggests data for basic interpretative research can be collected through interviews, observations, or document analysis.

Data for this study was mainly collected by means of interviews (through an online questionnaire and one-on-one interviews) with ten (10) online questionnaire participants. Further interviews of franchisors, franchise associations and financiers were also conducted. The data was collected over a period of two months. The questionnaire was distributed to all possible participants from the 01 December 2017 to 31 January 2018. The participants were asked to partake in the questionnaire and to also share the questionnaire link with other franchisees in their circle of contacts. A reminder to complete the questionnaire was sent to all possible participants in two-week intervals through

the various platforms used to reach franchisees. The interviews conducted were also done over the same period.

These data collection methods are discussed in further detail below.

3.3.1 Online questionnaire

In his article, Wright (2005) lists various advantages of conducting research using online based surveys and/or questionnaires. Some of the advantages listed are that online platforms allow access to unique populations that researchers would otherwise not have access to, they may save researchers time and money.

The data was collected using semi-structured interviews. In conducting this research an online questionnaire was constructed. The questionnaire consisted of 15 questions (refer to Appendix A). Another reason why an online questionnaire was considered to collect data is that it allows for both the collection of both qualitative and quantitative data for research purposes. The multiple-choice questions asked mostly captured the quantitative aspects of the research, whilst the open-ended questions captured the qualitative aspects of the research. The online survey allowed for participants to enjoy anonymity, hoping that this results in the participants being as honest and open as possible. An online questionnaire also meant that participants could respond to the questionnaire at a time and place convenient and most comfortable for them, if they had internet access.

Once the online questionnaire was ready for distribution and usage it was distributed to all potential participants via:

- a) Email: emails were sent to franchise associations and other support structures such as financiers (banks, DFIs and franchise associations) to request that they ask franchisees on their databases to complete the online survey.
- b) Social media: the link to complete the questionnaire was posted on social media sites such as Facebook, Instagram and LinkedIn where business interest groups have pages and/or accounts.
- c) Face-to-face requests: by attending conferences hosted by associations such as FASA, the researcher requested qualifying attendees to complete the survey.

SurveyMonkey was used to collate all the data and the reports produced by the platform were used to analyse the results.

3.3.2 Interviews with participants, franchisors, franchise associations and financiers

In addition to the online questionnaire, a ten of the participants provided their contact details in their responses and volunteered to be contacted for further discussion of their responses. Although it was with only ten participants that the researcher had additional discussions with on their responses, it was nonetheless useful to include the summary results of these additional one-on-one interactions in this study.

In addition to the franchisees, some franchisors, franchise associations and financiers were interviewed to gain additional insight into the franchise sector and particularly how the sector is funded and supported in South Africa.

Stuckey (2013) notes that there are three types of interviews for qualitative research, these being structured, semi-structured and narrative interviews. With a structured interview the questions asked are predetermined and asked in a predetermined order. The interviewer in this case sets the direction of the discussion. With semi-structured interviews the interviewer outlines the topic(s) to be discussed but the responses from the interviewee set the direction of the discussion. Narrative interviews are unstructured and typically have wide open-ended questions where the researcher focuses on the story of the participant and their life experiences.

The interviews conducted for this research paper were semi-structured to allow for a free interaction and expression on the open-ended questions but to still focus on the topic of equity contribution financing and its impact on the participants. The interviews with franchisors and financiers occurred at workshops, franchise conference and telephonically.

3.3 Sampling

Marshall (1996) states that there are three broad approaches to selecting a sample for qualitative research. These are the described briefly in the table below:

Table 5: Approaches to selecting a sample for qualitative research

Selection of sample approach	Description
Convenience sample	In this case the researcher selects the most accessible subjects to form part of the sample.

Judgement sample	This sampling technique is also known as purposeful sampling, the researcher actively selects the most productive sample to answer the research question. Factors that are likely to have an influence on the sample selected are the researcher knowledge of the research area, available literature, and evidence from the study itself.
Theoretical sample	Theoretical sampling necessitates building interpretative theories from the emerging data and selecting a new sample to examine and elaborate on this theory.

Merriam (2002) states that, for qualitative research, it is important to select a sample from which the most can be learned. To derive samples for this study, elements of both the convenience and judgement sampling method were used. It was judgement or purposeful sample because the online questionnaires were circulated to participants that met certain criteria i.e. were owners of franchises or had owned a franchise prior. The most accessible participants, either through online platforms, email, or telephonic access randomly formed part of the sample.

Online questionnaire sample

The sample was formulated through an online questionnaire, as the responses to the questionnaire were limited, all the responses received formed part of the sample if they passed the integrity checks criteria i.e. all fields completed correctly.

From Table 6, there were a total of sixty-nine (69) responses to the survey. All the 69 participants completed and submitted the questionnaire i.e. no participants started the questionnaire and abandoned it prior to submitting. The average time it took each participant to complete the questionnaire was five (5) minutes.

Table 6: Number of participants and time spent completing survey

Title of questionnaire	Total number of participants	Completion rate	Typical time spent
How franchisees raised the equity contribution required to purchase their first franchise?	69	100%	5 minutes

One-on-one interviews sample

Some of the participants of the online questionnaire responded that they would be available for further questions and discussion with the researched if requested. To gain additional insight, all those that offered their time to partake in one-on-one interviews were interviewed prior to the cut-off date of 31 January 2018. The responses of all ten participants to the one-on-one interviews formed part of the sample of the franchisee respondents. Due to time constraints it was not possible to include all online questionnaire participants in the interviews. Participants who consented to being interviewed after 31 January 2018 did not form part of the sample.

Additionally, the inputs from all other stakeholders such as franchisors, financiers and franchise associations were factored into the results of this study. Interviewees were selected from each stakeholder grouping to ensure that they are representative of the population.

3.4 Data analysis methods

The data analysis methods for both the quantitative and qualitative data collected are discussed below.

3.4.1 Quantitative data analysis

According to Blaikie (2003), there are four ways of analysing quantitative data. These are univariate descriptive analysis, bivariate descriptive analysis, explanatory analysis and inferential analysis. The univariate descriptive analysis is used to *represent* the characteristics of a phenomenon. The bivariate descriptive analysis is a step up from the univariate analysis in that it seeks to *establish either similarities or differences* between characteristics of certain groupings. An example would be grouping the answers of a certain range into categories and presenting these frequencies in pictorial or graphical format. Explanatory analysis goes beyond answering the “what” that boteh descriptive analysis does to explaining the “why”, dealing with the causation of a phenomenon. Inferential analysis is used when data collected from a sample is used to estimate the characteristics of the whole population.

The quantitative data collected in this research paper was analysed using the bivariate descriptive analysis method. The quantitative data was grouped into different categories such as gender, age and percentage equity contributions depending on the questions being asked. This made it possible

to establish differences or similarities between the different categories using measures of association and correlation.

3.4.2 Qualitative data analysis

Thorne (2000) acknowledges that although there are many qualitative data analysis computer programs available on the market today, these are essentially aiding in sorting and organising sets of qualitative data and none are capable of the intellectual and conceptualising processes required to transform data into meaningful findings.

There are two ways of analysing qualitative data. The first being the examination of findings with a predetermined framework i.e. the framework analysis (Pope, Ziebland, and Mays (2000). This approach involves the researcher first familiarising oneself with the raw data, then identifying a thematic framework i.e. identifying all key issues, concepts and themes and indexing these common themes accordingly. The second is a more exploratory approach, allowing one to code and consider all the data, thus allowing new interpretations to be formed. This is referred to as the “thematic network analysis, (Attride-Stirling, 2001).

For this study, the thematic network analysis method was used, as the qualitative data collected need to be analysed and interpreted without being boxed into a preconceived framework in order to fully understand the respondent’s individual experiences.

3.5 Research reliability and validity

Reliability

Reliability according to Saunders, Lewis, and Thornhill (2009) is referred to as “the extent to which your data collection techniques or analysis procedures will yield consistent findings” (p. 156). The online platform selected that would host the questionnaire is a reputable platform that has been used, tried and tested over many years and many surveys. It comes with the added advantage of having security aspects that ensure that participants are indeed persons and not “robots” or machines. In addition, the platform would run basic integrity checks to ensure that incomplete or incorrect responses are flagged and excluded from the results where necessary.

Validity

Saunders et al. (2009) list validity as being “concerned with whether the findings are really about what they appear to be about” (p. 157). There is a concern about reliability due to the lack of

standardisation of semi-structured interviews (Saunders et al., 2009). To address this threat the interviews conducted with franchisees were structured such that they followed the same format as the online survey which participants had already completed online. The interview schedule also allowed the interviewee to formulate their views; and become familiar with the type of issues being addressed. Maxwell (1996) also notes two threats of the inductive research methods: these threats being researcher bias and the influence of the researcher on the setting or individual being studied.

The fact that interview responses were written down, is a threat to validity. Hannabuss (1996) mentions, “disadvantages of written notes include memory lapses, inability to interpret notes and danger of imposing a false coherence or meaning on the material” (p. 28). To negate this threat, all the interview notes were read back to the participants for verification. Shenton (2004) refers to Lincoln and Guba’s consideration that “member checks”, which entails asking interviewees to read transcripts of dialogues in which they participated, to be the single most important provision to bolster a study’s credibility. This is intended for interviewees to consider whether their words match what they intended. According to Klassen and Le Blanc (1993), this verification method ensures that assembled data has the consent of those interviewed, allowing for no possibility that it could be disputed later.

Golafshani (2003) states that reliability and validity can be understood to be the trustworthiness, rigor and quality in qualitative research. To reduce researcher bias and increase the reliability and validity of research results, triangulation is recommended. Triangulation is a validity procedure where researchers search for convergence from different sources to formulate common themes or categories in a study (Creswell & Miller, 2000). Leech and Onwuegbuzie (2007b) refer to Maxwell’s theory that theoretical and interpretive validity is affected where a one-size-fits-all approach is used to analyse qualitative data – because of interpretations not being consistent with the underlying data. Leech and Onwuegbuzie (2007b) contend that to triangulate results, researchers need to use more than one data analysis tool. The researcher in this study used various data analysis techniques, such as summarising interview notes, constant comparison analysis and classic content analysis, to improve the rigor of the analysis and gain inferences from more than one vantage point.

3.7 Limitations

In his article, Wright (2005) also highlights some disadvantages of conducting online based research and online based surveys. In conducting this research, some of the above disadvantages

as cited by Wright (2005) were encountered. It was difficult to distribute the questionnaire link in bulk through online communities as a result of the privacy mandate that most have. Some potential participants were also sceptical on the use of the questionnaire results and were thus reluctant to complete the questionnaire. In addition, there were some limitations not noted by Wright (2005) that were encountered from selecting the online questionnaire as a primary method for data collection. These limitations are listed below:

a) Requirement for internet access

To partake in the questionnaire participants required internet access for at least ten (10) minutes.

b) As it is remote, the platform did not afford the participants an opportunity to ask clarification questions if they did not understand, thus leading to inaccurate responses

c) A few of the online platforms and communities stated that their constitution of the communities does not allow for questionnaires to be uploaded on their pages. This was experienced a lot with Facebook groups for small businesses and franchises in particular

d) Most organisations such as Franchise Direct and financial institutions such as ABSA were reluctant to provide the email addresses of their members and/clients as it was against company policy.

To address the above challenges, it became necessary to derive a social media strategy where platforms like LinkedIn were used where there are rules of participation, but these are not as restrictive. Word of mouth assisted a lot too in getting the questionnaire link distributed via friends, colleagues and professional associates.

3.8 Chapter summary

For this study, a mixed methods research strategy was adapted as a combination of both quantitative and qualitative data would address the research questions more comprehensively. In this chapter the embedded research design was outlined and justified. Additionally, the chapter also outlined the sampling techniques, data collection and data analysis methods used in this study. The strategy taken to ensure that data validity and reliability was maximised was outlined and the limitations of the research were discussed.

In the next chapter, the research findings are presented, analysed and discussed.

CHAPTER FOUR: RESEARCH FINDINGS, ANALYSIS AND DISCUSSION

4 Introduction

The findings below are drawn from both quantitative and qualitative data collected from an online questionnaire completed by both current and former franchisees who have operated and/or are operating a franchise in South Africa. A total of sixty-nine (69) participants completed the questionnaire and on average completed the questionnaire within ten (10) minutes. The questionnaire consisted of fifteen (15) questions (refer to Appendix A, of which three (4) were personal questions about the franchisee i.e. gender, race and age.

In order to contextualise the results of this study, it was firstly necessary to collect data on the franchisees, their franchise as well as the estimated amount that the franchisee had to raise as owner's contribution.

4.1 Demographics of participants

The participants were asked personal questions on gender, race and age. The demographic characteristics of participants are summarised below:

Table 7: Demographic characteristics of questionnaire participants

	Frequency	Percent (%) ¹
Gender		
Female	25	36
Male	44	64
Race		
White	29	43
Black/African	25	37
Coloured	4	6
Indian	8	12
Mixed race	1	1
Asian	0	0
Other	1	1
Current Age		
18-20 years	0	0
21-35 years	11	16
36-45 years	26	38
46-55 years	22	32
56-65 years	10	14

¹ Rounded off to zero decimals

Over 65 years	0	0
Age when respondent purchased first franchise		
18-20 years	0	0
21-35 years	31	45
36-45 years	23	33
46-55 years	14	20
56-65 years	1	2
Over 65 years	0	0

Bardasi (2008), in a questionnaire commissioned by the World Bank, found that African women are less likely to own a business than their male counterparts. This seems to be further demonstrated when looking at the fact that 64% of the participants to this research paper were male.

Constantaras (2017), in a survey conducted on franchisees in South Africa, noted that 86% of franchise owners were white. It would have been a reasonable conclusion for one to assume that most of the participants in this study would also be white. Interestingly, although most participants were indeed white (43%), black/African participants were not far behind at 37%, with 12% being of Indian descent.

Thirty eight percent (38%) of the participants were between the ages of 36-45 years and only 16% were below the age of 35. With the Seed Academy estimating that almost half of the unemployed are below the age of 35, it is encouraging to see that 45% of the participants were below the age of 35 when they purchased their first franchise.

4.2 Sectors that participants first franchise operates in

Table 8: Franchise Sectors

Answer choices	Responses (%)	Responses (No.)
Automotive products and services	1.45%	1
Building and home maintenance	1.45%	1
Business to business supplies	4.35%	3
Education and training	11.59%	8
Fast food/take out	14.49%	10
Health and Beauty services	5.80%	4
Real estate agencies	1.45%	1
Restaurants/sit down	10.14%	7
Retail incl. convenience stores	11.59%	8
Video rental and entertainment	1.45%	1
Petrol supplies	2.90%	2
Other (please specify)	33.33%	23
TOTAL	100%	69

Of the 69 participants, 25% are operating franchises that sell food, with 14.5% operating fast food/take out franchises. Of the 69 participants, 11.5% operate franchises within the retail sector.

The sector classifications used in the questionnaire are from the FRAIN (2004) guidelines, as seen in Appendix B: Table 2. It did however become apparent in analysing the results that the classifications were either incomplete or confusing for the participants as 23 of the participants (33%) chose to specify sectors other than the sectors mentioned above.

Ten (10) of the 23 participants are in financial services such as accounting, taxation and insurance. Financial services or business services

Four (4) of the 23 are in logistics, such as couriers’ services and shuttle services. Two are in telecommunications and one (1) in water filtration and purification and another one in private investigations.

Three (3) of the 23 participants stated that their franchises provide mobile coffee, quick service coffee and supply coffee to corporates. Providing mobile coffee could have been classified as fast food/take out, the same applies to “quick service coffee”. The supplying of coffee to corporates could have been classified as Business to business supplies or even fast food/take out.

The twenty-three (23) participants who selected other were then sorted into the other categories that closest matched the categories in the survey. In instances where they could not be classified into the existing categories, a new category was created. In the end, four (4) new categories were created to aid in analysing the results, these were:

- Financial services
- Private investigations
- Telecommunications and
- Water filtration and purification

Table 9: Sectors in which participants franchise operates

Sector	Responses (%)	Responses (No.)
Automotive products and services	7.25	5
Building and home maintenance	1.44	1

Business to business supplies and services	5.80	4
Education and training	11.59	8
Fast food/take out	18.84	13
Financial services (NEW)	14.50	10
Health and beauty services	5.80	4
Petrol supplies	2.90	2
Private investigations (NEW)	1.44	1
Real estate agencies	1.44	1
Restaurants/sit down	10.14	7
Retail, including convenience stores	11.59	8
Telecommunications (NEW)	2.90	2
Video rental and entertainment	2.90	2
Water filtration and purification (NEW)	1.44	1
TOTAL	100	69

From the summary of the results in Table 9 above, 29% (20 of the 69) of the participants operate franchises in the food sector, i.e. the combined results for fast food/take out and restaurants/sit down, followed by financial services at 14.5%.

4.3 South African province in which the franchise operates in

South Africa has nine (9) provinces. Of these nine provinces, Gauteng is the economic hub of the country. It comes as no surprise then that, as seen in Figure 3 below, 60.3% of the participants purchased their first franchise in Gauteng.

Kwa-Zulu Natal, geographically the largest of the nine provinces came in with 14.7% of the participants.

Three provinces are not represented in the participants to the survey, these being Limpopo, Mpumalanga and Northern Cape. As a result, the results presented here cannot be described as South African results as they do not include all nine provinces.

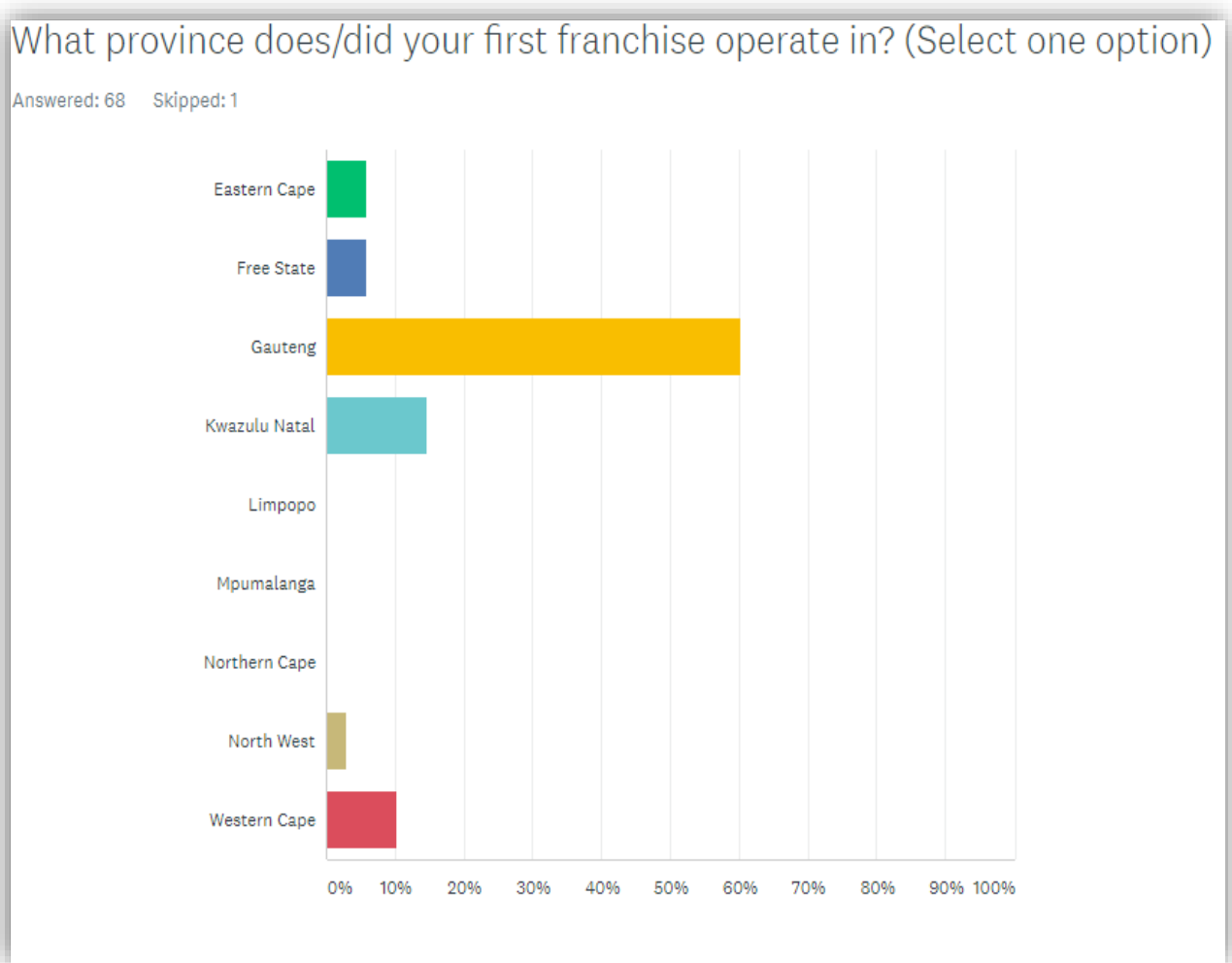


Figure 1: Province in which participants franchises operates

4.4 Length of time of the franchise operation

From Table 10 below, just over 70% (71.01%) of the participants first franchise was still in operation. This is commendable as a vast number of franchises and small businesses do not survive and cease operations.

Table 10: Is the franchise in question still in operation?

Answer choice	Responses (No.)	Responses (%)
Yes	49	71.01
No	20	28.99
TOTAL	69	100

From Figure 5, it is observed that for the majority of the participants (47.1%), their first franchise has been operating or operated for a period of three years or less. This study further reports that 58.9% operated for a period of five years or less, which is higher than the 31% reported by Constantaras (2017). Gates (1994) also reported that 65.3% of franchises survived beyond four years compared to 72% of independent business. It is difficult to draw any conclusions on this data compared to the data in this study as substantial time has passed i.e. 24 years since. In addition to just the passage of time the economics have also changed.

The remainder of the results are summarised below:

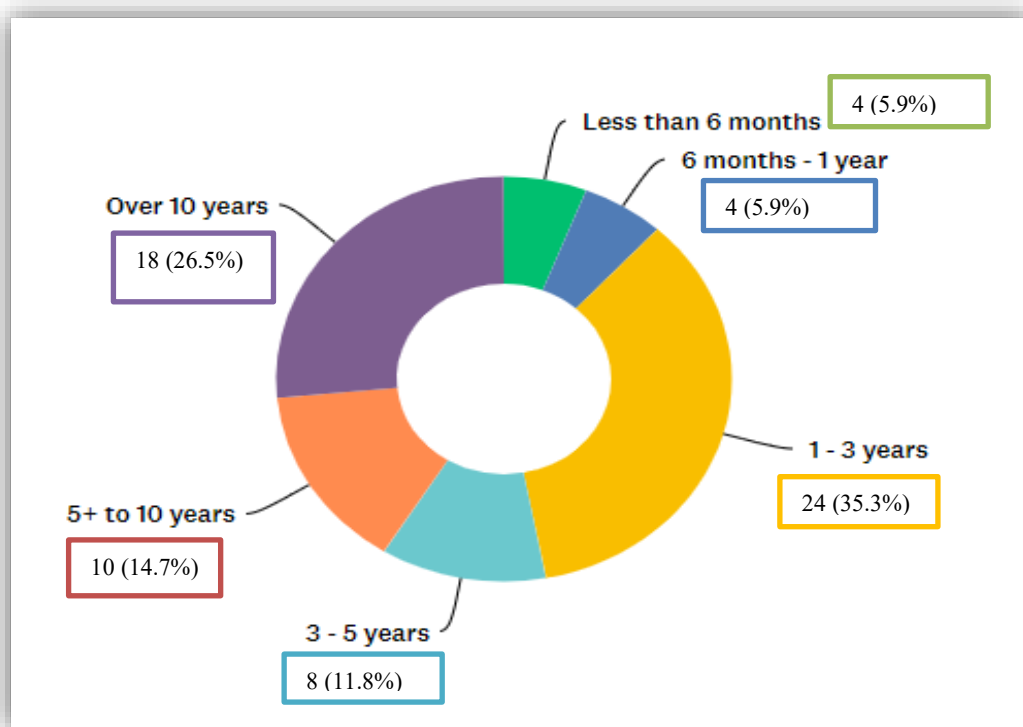


Figure 2: How long has your franchise been in operation?

4.5 Financing of the franchise

The results of the responses on the purchase price of the first franchise is presented in Table 12. On average, total purchase price of the participants first franchise was R878 261. This is the purchase price that the participants would have had to finance through debt or equity, or with a combination of debt and equity. According to Constantaras (2017), the average upfront fee, also referred to as the purchase price for franchises was R467 000. This is 47% higher than the average purchase price the participants in this study paid.

Table 11: Purchase price analysis

Purchase price (ZAR)	Responses (No.)	Responses (%)
1-100 000	16	23.19
100 001-300 000	8	11.59
300 001-500 000	8	11.59
500 001-750 000	11	15.94
750 001-1 000 000	5	7.25
1000 000-1 500 000	6	8.69
1 500 001-2 000 000	7	10.14
2 000 001-5 000 000	4	1.45
5 000 001+	4	1.45
TOTAL	69	100
<i>Average price</i>	<i>878 261</i>	

Table 13 below indicates that most participants (42.65%) had to finance more than 90% of the purchase price through unencumbered equity. To illustrate this point this would mean that the franchisee had to inject between R799 218 and R878 261 towards the start -up costs of their franchise (i.e. 91% to 100% of R878 261).

Over 51% (51.47%) of the participants had to raise more than half of the total purchase price through encumbered equity.

Table 12: Percentage (%) of purchase price being equity

Answer choices	Responses (No.)	Responses (%)
Less than 10%	6	8.82
11-20%	8	11.76
21-30%	6	8.82
31-40%	5	7.35
41-50%	8	11.76
51-60%	1	1.47
61-70%	3	4.41
71-80%	1	1.47
81-90%	1	1.47
91-100%	29	42.65
TOTAL	68	100

4.6 Sources of the unencumbered equity required

Now that the amounts have been quantified and contextualised. The questionnaire sought to understand *how* or from what sources did the participants raise the unencumbered equity contribution.

The results are summarised in Table 14 below:

Table 13: Sources of equity

Source	Responses (No.)	Responses (%)
Personal savings	41	59.42
Family	11	15.94
Friends	2	2.90
Other business partners	12	17.39
Venture capital firm	0	0
Other (please specify)	3	4.35
TOTAL	69	100%

Most participants (59.42%, i.e. 41 participants) raised the equity from personal savings. These personal savings included, but were not limited to provident funds, pension funds and liquidation of investments like the sale of shares in companies.

Twelve (17%) of the participants financed the equity contribution through other business partners. To raise finance, a franchisee can instead of being the sole shareholder in a franchise, invite additional people to be shareholders, in exchange for a stake/shareholding, these partners would contribute towards the equity.

Eleven (16%) of the participants financed their equity through funds from family.

As seen in Table 15 below, for 50% of the participants it took less than six months to raise the required unencumbered equity.

Table 14: Length of time it took to raise equity

Answer choices	Responses (No.)	Responses (%)
Less than 6 months	34	50.00
6 months to a year	10	14.71
1-3 years	8	11.76
3-5 years	2	2.94
5-10 years	4	5.88
10-15 years	5	7.35
15-20 years	1	1.47
Over 20 years	4	5.88
TOTAL	68	100%

The last three questions of the questionnaire (Question 13, 14 and 15) were qualitative in nature. Interestingly, eleven (11) of the participants in the survey left their contact details such as emails and contact numbers in some of their responses so that the researcher could get in touch with them should they wish to discuss certain things further.

The results of the remaining questions in the questionnaire that are analysed in detail below are thus a combination of the responses from the online survey and telephonic and email discussions had with the eleven participants.

Question thirteen (13) of the questionnaire asked the participants what challenges they faced in raising the equity capital required. It is worthwhile noting that five (5) participants skipped Question 13.

The remaining sixty-four (64) participants outlined various challenges that they faced. In analysing the responses, it became necessary to categorise the challenges identified. The challenges fell into the broad categories outlined below:

Table 15: Categories of challenges faced by participants

Category	Description	No. of challenges	% contribution per category
Financial challenges	Financial challenges are these challenges that affected the financial position of participants and/or their franchise. These challenges are monetary and can be quantified either to an exact figure or reliably estimated.	27	31%
No challenges	This captures the responses from those participants that experienced no challenges	25	29%
Personal challenges	These challenges are those the franchisee faced at an individual level.	22	26%
Business challenges	These challenges are those that affected the set-up of the franchise. Be it the directors/shareholders composition of the franchise, the legal status or registration of the franchise and other business administration challenges.	10	12%
Family and friendship challenges	This category looks at the challenges that involved family and/or friendship relations.	2	2%
TOTAL		86	100%

Financial challenges

Financial institutions mandate

Traditional financial institutions such as banks were unwilling to assist in injecting equity into franchises, particularly if the application was not within a specified threshold with regard to the size of the applications. Some participants indicated that even government institutions were reluctant to inject equity into start-up franchises as their mandate did not include start-ups.

Financial institutions red tape

Where there was a willingness to fund the franchisees equity contribution, the process was lengthy and laden with red tape.

Collateral/surety

Even once the franchisee had managed to gather all the required information, some financial institutions still required collateral. The participants noted that their financial position did not allow them to have the required asset base that can be used as collateral.

Track record/experience

The lack of a track record counted against participants when approaching potential funders. Financial institutions would want to use past performance such as financial statements, feedback from customers and other creditors, to assess risk. As first-time franchisees, it is not possible to produce these and thus the applicant is automatically perceived as risky.

Liquidation of long-term assets

Some participants had challenges with liquidation of long-term assets. The sale of assets such as cars, property and shares or stocks can take some time. Some participants even resorted to selling assets at discount prices in order to free up cash for their equity contribution to the franchise purchase price.

Unpredictable cashflows (revenue), vs. constant loan and interest repayments

Participants also pointed out the challenge of having to balance unpredictable cash inflows into the business against the loan and interest repayments due to financiers. At the point of applying for finance franchisees had to ensure that they do not burden the franchise with too much debt as the debt repayments were not as flexible as those from equity.

No challenges

Interestingly, most the participants that said that they did not experience any challenges with sourcing the required equity were those that received funding from personal savings or from family and friends. One of the things they attributed this to was the fact that the friendship was long standing and thus the friend was lenient towards the franchisee.

Two of the respondents that experienced no challenges sourced their equity funding from the franchisor.

Personal challenges

Saving

A common theme amongst responses that financed their equity through personal savings was the difficulty of saving. Saving required one to be disciplined in their approach as sacrifices of non-essential items would need to be made to accomplish the savings goal. In some instances, savings targets could not be reached as result of unforeseen personal expenses.

In addition, some participants not only had to look after the needs of their immediate family members but extended family members too, making having money to save at the end of the month difficult.

Anxiety from lack of security

Those candidates that used their pension payouts upon leaving their jobs stated that they suffered from anxiety about their future i.e. whether they could have sufficient money to sustain themselves through retirement.

Franchisee Experience

The experience of the franchisee in business and in the sector that they wanted to operate a franchise in is seen as favourable towards a finance application. A key area of expertise that participants viewed as important was financial management. Some participants had working experience but did not have financial management experience or the sector experience to assure potential financiers that they would be successful in running the franchise.

A participant also pointed out that they believe it takes a certain personality and confidence to be able to convince possible financiers of a business opportunity and that one cannot be shy or reserved otherwise they will not succeed in convincing others of the opportunity they present.

Franchisee background

Some participants felt that their background, be it race, gender, age, education levels, place of birth contributed to their struggle in accessing finance. As a result, one participant had to downplay their education level in order to access donor funding from a European DFI. This said DFI had a funding programme earmarked for to get those that don't have formal education into business.

Business challenges

Suitable business partners

Some of those participants that financed their equity through getting other business partners into their franchise indicated that it took some time and effort to find suitable interested business partners to inject equity into the franchise.

Delays in anticipated timelines

Another challenge that was highlighted was the timelines. Participants indicated that they had to delay their start-up of the franchise until such time as they were able to raise equity. This led to loss of preferred sites in some instances.

Compilation of a business plan

In order to approach potential funders potential franchisees had to draft a business plan. Various information needs to be contained in the business plan such as sector/market analysis, financial projections and SWOT analysis. Some respondents indicated that were not able to draft these business plans themselves and had to source the services of consultants to assist them in drafting their business plans. The amount of time it took to draft these business plans added to the amount of time it took participants to raise capital. In addition, where participants outsourced the drafting of their business plans, this further increased their franchise start-up costs.

Lack of support from franchisor

In responding to queries on the business proposal from potential funders, franchisees were required to answer some questions on the franchise opportunity. This information is often in the possession

of the franchisor. It became difficult for some participants to get access to information from franchisors, leading to the process of say drafting a business plan to be prolonged.

Family and/or friendship challenges

One of the participants responded that they experienced challenges in convincing family members to loan them money. The participant attributed this to the fact that the family members knew them well and were sceptical that they would get their money back as they knew the lifestyle of the participant.

Once the participants got the opportunity to list the challenges, they faced in sourcing equity finance for their franchises, the questionnaire sought to understand the impact the challenges had on themselves, their friends and family as well as their franchises.

Sixty two (62) of the sixty nine (69) participants responded to this question. In order to analyse the responses from participants, the responses were grouped into four main categories, namely negative impact, positive impact and neutral or no impact.

Table 16: Impact of the challenges faced by franchisees

Impact of challenge(s)	No of responses	% contribution
Negative impact	38	61%
No or neutral impact	17	27%
Positive impact	7	11%
TOTAL	62	100%

Negative impact

The negative impacts that participants noted were working long hours in order to generate sufficient savings. This took away from spending time with family and friends, leading to stress and strained personal relationships. There were also instances where the participants defaulted on payments to family and friends which led to strained relations with the greater family or friendship network. In some instances the relationships were broken beyond repair where it ended up with the parties taking each other to court. Some participants pointed out that they also put the family residence up as collateral, leading to ongoing disagreements at home, particularly where there was a threat that the franchise will not do well (thus exposing family home and funds to risk). The utilisation of all savings led to instances where participants had no funds when emergencies occurred and had to rely on further debt to get by. Franchisees are then over exposed to debt, further compromising

their financial position. The participants in some instances had to change their lifestyle and “downgrade” to smaller apartments, cheaper cars and cut back on holidays in order to raise capital. For some, the cashflow challenges experienced by the franchise lead to the failure of the franchise. The revenues generated by the franchise were not enough to pay off all the debt within the franchise and to also meet the cash flow demands from the borrowings from family and friends. Participants pointed out they lost the power to make decisions about their franchise as those that financed their equity, such as the franchisor would then want to make all the decisions pertaining to the direction that the franchise should take, particularly where there was a threat that the franchisee would not be able to meet their debt obligations to the financier.

No or neutral impact

There were those participants that did not experience any challenges in sourcing equity from their franchises. The participants that felt that the challenges had no impact on them or their franchises were those that fell into this category.

Positive impact

Not all the impacts of the challenges was negative. Some of the positive impacts that participants experienced are that the source of finance for their own contribution increased their drive and will power to continue pursuing their dream, especially that they now had “skin in the game” as they had used their own financial resources. The support of family and friends who were willing to assist with financing the franchise strengthened relations for some participants as they realised that their family and friends can be relied on in times of need. Some of the participants that were financed by their franchisor stated that their financial challenges strengthened the franchisor/franchisee relationship as they felt that the franchisor was supportive and thus they as the franchisee felt the need to be loyal to the franchise. The challenges experienced by some participants forced them to seek other shareholders for their franchise. The introduction of the new shareholders had advantages for the franchise as they brought with them experience and ideas that were used to improve the performance of the franchise.

In conclusion, **Question fifteen (15)** of the questionnaire asked the participants, what advice they would give to other aspiring franchisees with regards to raising equity finance for their franchises. Of the 69 participants that took part in the survey, 63 participants (91.3%) responded to this question.

The summary of responses on advise for potential franchisees is outlined in Table 18 below.

Table 17: Advice to potential franchisees

Advice	Explanation of advice
Business advice	<p>An estimated 10% of the participants felt its better for aspiring entrepreneurs to build their own brand, no matter how long it takes. Even if this means starting small and building from scratch. These participants found the purchase price of a franchise to be expensive and felt it would have been cheaper to start a business outside of the franchise model.</p> <p>Do detailed research on the franchise before investing, pay particular attention to the projected cash flows which are not always as great as the franchisor states. Ensure that you complie a deatiled buiness plan and that you fully understand all its contents. Ensure that your franchisor has a solid track record.</p> <p>Read the fine print of all contracts, even sourcing legal advice. It will be worth it in the long-term. Focus on the royalties and other franchise related expenses as these can drain the business resources.</p> <p>Request as much assiatnce as possible from the frachisor, they ofetn have networks that can assist with funding as well.</p> <p>Be open to the idea of getting additional like minded partners or sharehodlers onboard to sahre respinsibilites with</p> <p>Ensure that you have sufficnt cahs available to sercive at least six (6) months of the franchises obligation</p> <p>Speak to other franchisses underthe franchise that you have interst in. if possible get a mentor that will walk the jourey with you</p> <p>Know that you will need to be actively involved in your franchise and will not be abke to simply leave this to a manager or staff, be preapred for the long hours involved</p>
Financial advice	<p>Start saving as much as you can as early as you can and avoid using your pension where possible</p> <p>Use as much cash of your own as possible instead of taking loans. Try and fund over 90% of tehstart up cots with equity and not debt</p>

	<p>Do not take on too much debt, over gearing the business will put pressure on the sustainability of the business</p> <p>Try crowdfunding</p> <p>To reduce the start up capital expenditure of starting a franchise purchase these capital items at auctions</p> <p>Develop a strong relationship with the franchise banker so that they can provide you with some financial advice on being a franchisee</p>
Personal advice	<p>Be disciplined and consistent in pursuing your goals. Ensure that these goals are realistic.</p> <p>Expect the best but prepare for the worst so do not invest monies you cannot afford to lose.</p> <p>Remain ethical and true to your beliefs at all times, even when you are desperate.</p> <p>Be patient, especially when dealing with state institutions who often have long and slow processes in assessing applications.</p>
Family and friends	<p>Ensure that your family and friends understand that the first three years may be tough and that they are adequately prepared for it. Do not promise that you will pay back the money you borrowed within a short space of time as this is very unlikely with most franchise businesses</p>

4.7 Conclusion

The research conducted demonstrated that franchising is still an attractive entry point into business across demographics. Sixty four percent of the 68 participants were male and only 16% were below the age of thirty five (35). This demonstrates that more needs to be done to encourage women and youth to participate in the ownership of franchises.

The next chapter of this study summarises conclusions from the results analysed in this chapter and provide some recommendations on how the challenges identified in Chapter Four can be addressed by the various stakeholders. In addition, some recommendations on future research are made in order to address some of the limitations of existing literature on franchise funding and some limitations of this study.

CHAPTER FIVE: RESEARCH CONCLUSIONS AND RECOMMENDATIONS

5. Introduction

This chapter summarises the findings of the research conducted as well as provide policy recommendations in addressing the difficulties that franchisees face in raising equity contributions.

5.1 Summary of findings and conclusion of study

This study has highlighted that the franchise business model continues to be used by entrepreneurs and thus does have some advantages. There a few participants to the survey that suggested that, although franchising does have attractions, it's important that those wanting to enter the business world do not focus so much on franchises that they neglect to explore other ways of entering the market.

Raising equity finance is still a challenge for a lot of franchisees as financial institutions still require a large portion of the franchise to be financed by the franchisee. A vast majority of participants financed their required equity to personal savings and soft loans from family and friends

5.1.1 Unencumbered equity requirements

Over 51% of participants had to contribute more than 50% of the franchise purchase price as unencumbered equity. On average this means that participants had to raise an estimated R439 130 as unencumbered equity. Forty-four (44) of the sixty-nine participants i.e. 64.17% raised this unencumbered equity in less than a year. Interestingly, over 70% of these participants financed the required equity from savings.

Through the interviews conducted with the participants through email and telephonically, it was discovered that participants only counted the period that they contacted their bankers, or pension fund managers to when they received the cash. The true period to raise this funding would have to be calculated from when one starts saving to when one accesses the funds. To illustrate, if a participant used their pension fund pay-out, they would need to count the number of years from when they started working and contributing to their pension funds until the point that they cashed out, not merely calculating from when they retired and completed forms to draw on their pension funds. The researcher only had follow-up interviews with ten of the participants but it is very likely that more participants interpreted this question the same way. If this is the case, this would mean that most participants likely took longer than a year to raise the required unencumbered equity.

5.1.2 Sources of unencumbered equity contribution and the implications thereof

Most participants (59%) financed this unencumbered equity requirement through personal savings such as retirement packages, cashing out pension funds and/other savings. The main implications for those that used their savings were mainly personal emotional strain caused by anxiety about the future should the franchise not succeed. In addition, family relationships were strained as spending patterns had to change as result of having contributed savings to the franchise venture. Things like holidays and other luxuries had to be forfeited. Some families even had to downsize on their homes to reduce household expenses.

The other prominent sources were other business partners (17%) and family (16%). Notably those that financed their equity contribution through other business partners and family did not report personal emotional challenges. Those that financed their unencumbered equity through other business partners reported some positive implications such as having access to additional expertise in the franchise. The introduction of other business partners also brought about some additional discipline to how the participants handed the affairs of the franchise as the business partners provided some oversight. Those participants that received finance from family mostly viewed this assistance as soft loans, thus they did not feel pressure to repay these loans within the stipulated/agreed time, even with loan agreements having been signed by the parties.

5.2 Stakeholder recommendations

In making recommendations based on the results of this research paper, the recommendations are grouped into:

- practical recommendations that can be applied by franchisees, prospective franchisees and financiers.
- policy recommendations that can be applied by those tasked with drafting SMME policies and
- theoretical recommendations for future research

5.2.1 Practical recommendations

Personal and financial counselling

Existing and prospective franchisees should consider seeking personal and financial counselling to assist them and their families in adjusting to the pressures that come with being a franchisee.

Financier engagement

Existing and prospective franchisees should also continuously communicate with the funders, keeping them abreast with all franchise developments, especially those that may lead to them being unable to meet their financial obligations to their funders. Franchisees should especially not neglect to do this if the funders are family or friends.

Build a robust business plan i.e. plan for the periods where little or no revenue is generated

Prospective franchisees need to devise a robust business plan and action plans with various sensitivities. In instances where the franchise is not doing well for extended periods as an example, the franchisee must plan on how the cash required to fund fixed costs will be funded. If cash reserves need to be built into the business plan and operation for six or even twelve months, this will need to be done before a franchisee can start extracting dividends from the franchise.

Capacity building by financial institutions

Financial institutions benefit from the success of franchises. These benefits come in various ways such as the timeous payment of the loan repayment due to them. The growth of the franchise increases the chances of the franchise requiring additional finance going forward, thus recurring business for financiers. Financial institutions should therefore offer franchisees the financial skills that they often lack in running a franchise.

Franchisors reduction in equity requirements

Some franchisors in screening their potential franchisees require at least a 50% equity contribution upfront. The reduction of this to between 20 to 25% could greatly assist potential franchisees in entering the market. The balance of the equity requirements can be “made up” by franchisors taking an equity stake in franchises or having the equity being paid through a profit-sharing arrangement. Some participants, albeit a small number indicated that they received financial assistance from franchisors to assist with the required levels of equity in the franchise and they viewed this as one of the factors that lead to the success of their franchise.

Reduction in royalties

The royalties that franchisors demand can be excessive at times and the reduction of these would improve the cash position of franchisees. In order to make up for the returns that will be lost from reduced royalties, franchisors can increase the length of the franchise agreements with franchisees.

5.2.2 Policy recommendations

Provision of grants

The South African government could look at initiatives to assist franchisees in raising the requisite equity contribution. This could come in the form of **grants** for qualifying franchises and franchisees. In order to incentivise the franchisee to do well, these grants could be conditional. As an example, the grant would be repaid back to the government should the franchisee not achieve some agreed KPI's. This will ensure that potential franchisees do not deplete their retirement savings pursuing the franchise venture.

Compulsory personal and financial counselling by all financiers, franchisors and other stakeholders

Government can also introduce initiatives such as workshops with franchisees on managing the stress and anxiety that can potentially arise because of the franchise venture. The workshops would also need to include an education drive for the family, friends and business partners of the franchisee so that they know and understand how they will be impacted.

5.2.3 Recommendations for future research

The main data collection method used in conducting the research contained in this research paper was an online survey. Surveys, particularly online surveys are good tools to reach a widely geographically distributed target audience, but online surveys do have inherent shortcomings. Consequently, some recommendations for future research on this area are outlined below.

5.2.3.1 One-on-one, face-to-face interviews of franchisees

As the research in this paper and the results thereof was done via an online survey, one-on-one, face-to-face interviews with participants could provide additional insight on this piece of research.

Benefits for questionnaire owner/researcher and participants

It would provide an opportunity to explain the questions posed. Some participants in the questionnaire did not respond to all the questions, as a result their responses were excluded from the results. A possible reason for participants leaving out certain questions may be that they did not understand the questions and/or context in which they were asked. One-on-one interviews would

possibly increase the level of participation, as the interviewer would be able to provide clarity where the participant requires it.

The interviewer also has an opportunity for follow-up questions to responses.

Participants had the opportunity to ask clarification questions.

5.2.3.2 Questionnaire inclusive of all nine provinces of South Africa

In this research paper, three provinces, namely Mpumalanga, Limpopo and the Northern Cape are not represented in the sampled participants.

A questionnaire inclusive of these provinces could shed additional light on how franchisees in these regions financed their franchises.

5.3 Conclusion

This chapter gave a summary and conclusion of the study. The chapter also provided some policy recommendations that can be implemented by policy makers and formulators in South Africa. It finally provided the suggested recommendations for future research in an endeavour to provide effective empowerment of existing and potential franchisees in South Africa. This is done with the hope that all interested stakeholders can utilise the findings of this study to facilitate an easier entry into the franchise sector, particularly in South Africa.

REFERENCES

- ABSA Franchising. (2015). *Principles of Franchising*. Retrieved from: <https://www.scribd.com/document/305061393/Principles-of-Franchising>
- Bardasi, E. (2008). *Gender, Entrepreneurship, and Competitiveness, Results from enterprise questionnaire data*. PRMGE, The World Bank
- Bates, T. (1994). A comparison of franchise and independent small business survival rates. *Small Business Economics*, 377-388.
- Bernard, H.R. (2017). *Research Methods in Anthropology: Qualitative and Quantitative Approaches*. Lanham, Maryland: Rowman & Littlefield.
- Blaikie, N. (2003). *Analysing quantitative data from Descriptive to Explanation*. Thousand Oaks, CA: SAGE Publications.
- Bureau for Economic Research (BER). (2016). *The small, medium and micro enterprise sector in South Africa*. Stellenbosch: University of Stellenbosch.
- Business Live. (2014). *Retrenchments at 10-year high as economy sheds jobs*. Retrieve from <http://www.bdlive.co.za/economy/2014/02/11/retrenchments-at-10-year-high-as-economy-sheds-jobs>
- Business Tech. (2017). *How much it costs to open a top franchise in SA and how much you can earn*. Retrieved from: <https://businesstech.co.za/news/business/196138/how-much-its-costs-to-open-a-top-franchise-in-sa-and-how-much-you-can-earn/>
- Cambridge Dictionary. Retrieved from: <http://dictionary.cambridge.org/dictionary/english/finance>
- Chen, J. (2019). *What is debt?* Retrieved from: <http://www.investopedia.com/terms/d/debt.asp>

Constantaras, M. (2017). *The South African Franchisee.*,
<https://mail.google.com/mail/u/0/?tab=rm&ogbl#inbox/FMfcgxwHNMZTtHwQnSTbDmNvXDLZdL?projector=1&messagePartId=0.2>

Creswell, J.W. & Miller, D.L. (2000). *Determining validity in qualitative inquiry. Theory into Practice.* Ohio: The Ohio State University, College of Education.

Creswell, J.W. (2011). *Educational research.* New Delhi: PHI Learning Private Limited.

Creswell, J.W., & Plano Clark, V.L. (2011). *Designing and conducting mixed methods research* (2nd ed.). Thousand Oaks, CA: Sage Publications.

Dawson, A. (2018). *South African Franchise Industry Outlook for 2018.* Retrieved from:
<https://www.franchisedirect.co.za/information/south-african-franchise-industry-outlook-for-2018>

Elomo, P.N. (2014). *Determinants of capital structure of start-up firms in South Africa* (MMFI Dissertation). Retrieved from:
<https://pdfs.semanticscholar.org/3827/91d7279edccd20f1acc3e79e46d984b19c97.pdf>

FASA (The Franchise Association of South Africa). (2016). *Annual Report 2016.* Retrieved from: www.fasa.org.za

FASA (The Franchise Association of South Africa). (2017). *Franchise Grows in a Tight Economy.* FASA. Retrieved from: <http://fasa.co.za/fasablog/franchise-grows-tight-economy/>

FASA (The Franchise Association of South Africa). (n.d.). *Franchising Help Desk.* Retrieved from <https://www.fasa.co.za/franchising-help-desk/#1553692556862-42dc9f70-495d>

FRAIN (2004). *Franchise Census 2004.* FRAIN, Pretoria.

Franchise Direct. (2011). *History of franchising in South Africa decade by decade.* Retrieved from:

<http://www.franchisedirect.co.za/information/aboutfranchisinginsouthafrica/historyoffranchisinginsouthafricadecadebydecade/285/1381/>

FranChoice Blog. (2018). The history of franchising. Retrieved from:

<http://www.franchoice.com/franchise-information-guide/what-is-franchise/history-of-franchising>

Gikonyo, L., Berndt, A. & Wadawi, J. (2015). Critical Success Factors for Franchised Restaurants Entering the Kenyan Market: Franchisors' Perspective. *Sage Journals*, 5(4). doi: 10.1177/2158244015614378

Golafshani, N. (2003). Understanding Reliability and Validity in Qualitative Research. *The Qualitative Report*, 8(4), 597-606.

Retrieved from: <https://nsuworks.nova.edu/tqr/vol8/iss4/6>

Hannabuss, S. (1996). Research Interviews. *New Library World*, 97(1129), 22–30.

Haron, H., Said, S.B., Jayaraman, K., & Ismail, I. (2013). Factors influencing small medium enterprises (SMES) in obtaining loan. *International Journal of Business and Social Science*, 4(15), 182–195.

IHS Economics. (2014). *Franchise Business Economic Outlook for 2014*. Report prepared for International Franchise Association Educational Foundation. September 2014 update.

IHS Economics. (2016). *Franchise business outlook for 2016*. Report prepared for International Franchise Association Educational Foundation.

Illetschko, K. (2002). *How to evaluate a franchise*. Pretoria: The franchise Association of South Africa.

Illetschko, K. (2005). *How to franchise your business*. Johannesburg: The franchise Association of South Africa.

Kauffmann, C. (2005). *Financing SME's in Africa*. African Development Bank and the OECD Development Centre. Policy Insights No 7.

Kenneth F.H. (2000). Recognizing deductive processes in qualitative research. *Qualitative Market Research: An International Journal*, 3(2), p. 82-90. doi: 10.1108/13522750010322089

Klassen, T., & Le Blanc, S. (1993). Methodological Issues in sociological research on Public Policy: Utilizing interviews. *Society/Societe*, p. 22-26.

Kunzemann, T. (2010). *Microfinance: Do you susu?* Retrieved from:
https://www.allianz.com/en/about_us/open-knowledge/topics/finance/articles/100220-microfinance-do-you-susu.html/

Kurt, D. (2019). *What is finance?* Retrieved from:
<http://www.investopedia.com/ask/answers/12/finance.asp#ixzz4qR34H6Sa>

Larson, G. (2012). A Needle in a Haystack: How a New Tool Is Unlocking Entrepreneurship in Africa. *Harvard Kennedy School Review*, XII, 76–80. Retrieved from:
<https://www.harvardkennedyschoolreview.org>

Lee, Y. (2014). *Insight for Writing a Qualitative Research Paper*. Iowa: Iowa State University.

Lewis, J. (2009). *Business viability: A comparison between franchises and independent businesses*. (Masters Dissertation). Retrieved from:
https://pdfs.semanticscholar.org/7218/5435cfd035d3a1ca91ed5446bcfdd29eee0a.pdf?_ga=2.230291868.1813206316.1596020707-516740056.1596020707

Macleod, G. (1999). *Starting your own business in South Africa*. Cape Town: Oxford University Press Southern Africa.

Marshall, M.N. (1996). Sampling for qualitative research. *Family Practice*, p. 522-525.

Maxwell, J.A. (1996). *Qualitative research design*. Thousand Oaks, CA: Sage Publications.

Morse, J., Barrett, M., Mayan, M., Olson, K. & Spiers, J. (2002). *Verification Strategies for Establishing Reliability and Validity in Qualitative Research*. University of Alberta, Edmonton, Alberta, Canada: International Institute for Qualitative Methodology.

Murray, F. (2017). *South African Food Service industry report for 2016*. Retrieved from: <https://www.franchisedirect.co.za/information/southafricanfoodserviceindustryreport2016/>

Mutoko, W.R., & Kapunda, S.M. (2017). Factors influencing small, medium and micro-sized enterprises' borrowing from banks: The case of the Botswana manufacturing sector. *Acta Commercii*, 17(1), a426. doi: 10.4102/ac.v17i1.426

Nafu Farmer, (2008). *The basics of small business loans* . Retrieved from: https://journals.co.za/docserver/fulltext/ac_nafu/2008/12/58.pdf?expires=1596376314&id=id&acname=guest&checksum=9F719AFC40C1C0F4745C9F5297C54638

Nathan, G. (2006). *The Psychology of the Franchise Relationship*. Paper presented at the American Bar Association 29th Annual Forum on Franchising.

National Treasury, Republic of South Africa. (2016). *Budget Review*. Retrieved from: <http://www.treasury.gov.za/documents/national%20budget/2016/review/FullReview.pdf>

NKC African Economics, South Africa. (2017). *Quarterly update on South Africa; June 2017*.

OECD iLibrary. (2016). *Entrepreneurship at a Glance*. Retrieved from: http://dx.doi.org/10.1787/entrepreneur_aag-2016-en

Olufisayo. (2011). *Understanding owners' equity*. Retrieved from: <http://www.entrepreneurshipsecret.com/understanding-owners-equity/>

Pascua, S. (2014). *Monitoring, Evaluation, Accountability and Learning (MEAL) 6 Methods of data collection and analysis*. . The Open University

Patton, M.Q. (2002). *Qualitative evaluation and research methods* (3rd ed.). Thousand Oaks,

CA: Sage Publications.

Policy Board for Financial Services and Regulation. (2001). *SME's access to finance in South Africa – a supply-side regulatory review*. Retrieved from: <file:///C:/Users/Clarina/Downloads/Access%20to%20Finance%20in%20South%20Africa%20-%20A%20Supply-Side%20Regulatory%20Review.pdf>

Pope, C., Ziebland, S., & Mays, N. (2000). *Qualitative research in health care Analysing qualitative data*. Retrieved from: <https://www.ncbi.nlm.nih.gov/pmc/articles/PMC1117368/pdf/114.pdf>

Pretorius, M. & Shaw, G. (2004). Business plans in bank decision making when financing new ventures in South Africa. *South African Journal of Economic and Management Sciences*, 7(2), 221-241.

Prinsloo, J.W. (2000). *The saving behaviour of the South African economy*. Occasional paper no 14 in South African Reserve Bank.

Quartey, P. (2007). *Financing the growth of SMEs in Africa: What are the constraints to SME's financing within ECOWAS?* Review of Development Finance 7, Africagrowth Institute.

SA Good News. *Strong outlook for the South African franchise industry*. Retrieved from: <http://www.sagoodnews.co.za/categories/27-private-sector-a-business/6223-strong-outlook-for-the-south-african-franchise-industry.html>

Shenton, A.K. (2004). Strategies for ensuring trustworthiness in qualitative research projects. *Education for Information*, 22, 63-75.

Sogorb-Mira, F. (2002). On capital structure in the small and medium enterprises: the Spanish case. Retrieved from: https://papers.ssrn.com/sol3/papers.cfm?abstract_id=277090

Sophy, J. (2015). *Franchise Businesses Continue Rapid Growth Despite Concerns*. Retrieved from: <http://smallbiztrends.com/2015/01/franchise-business-growth.html>

StatsSA (2019). *Quarterly financial statistics*. Retrieved from:
<http://www.statssa.gov.za/publications/P0044/P0044March2019.pdf>

StatsSA. (2016). *Quarterly Labour Force Survey*. Retrieved from:
<http://www.statssa.gov.za/publications/P0211/P02111stQuarter2016.pdf>

Stuckey, H. (2013). *Three types of interviews: Qualitative research methods in social health*. Department of Medicine and Public Health Sciences, Pennsylvania State University College of Medicine, PA 17033, USA.

Subedi, D. (2016). Explanatory Sequential Mixed Method Design as the Third Research Community of Knowledge Claim. *American Journal of Educational Research*, 4(7), 570-577. doi: 10.12691/education-4-7-10

Tatham, R.L., Douglas, R., & Bush, R. (1972). An Analysis of Decision Criteria in Franchisor/Franchisee Selection Processes. *Journal of Retailing*, 48.1, 16-21, 94.

The ins and outs of raising money from friends and family. (n.d.). Retrieved from:
<https://www.entrepreneur.com/article/228103>

The Seed Academy. (2015). *First Annual Start-up Questionnaire Results 2015*

The Seed Academy. (2016). *Second Annual Start-up Questionnaire Results 2016*

Thorne, S. (2000). *Data analysis in qualitative research*. Vancouver, Canada: University of British Columbia.

Twin, A. (2019). *What is a refinance?* Retrieved from:
<http://www.investopedia.com/terms/r/refinance.asp>

Unencumbered funds unravelled. (n.d.). Retrieved from:

<http://www.entrepreneurmag.co.za/advice/franchising/franchisee-advice/unencumbered-funds-unravelled>

Walker, J. (2016). *How to spot the ideal international franchisee*. Franchising World . Retrieved from : <https://www.franchise.org/franchise-information/international/how-to-spot-the-ideal-international-franchisee>

Walters, C. (2001). Assumptions of qualitative research methods. *Perspectives in Learning*, 2, 60.

Which Franchise. (n.d.). *Common financial mistakes made by new franchisees*. Retrieved from: <https://whichfranchise.co.za/common-financial-mistakes-made-new-franchisees/>

Which Franchise. (n.d.). *Franchise finance*. Retrieved from: <https://whichfranchise.co.za/franchise-finance/>

Which Franchise. *Past Q&A from potential franchisees*. Retrieved from: <http://www.whichfranchise.co.za/past-ask-the-expert-questions-from-potential-franchisees/>

Wright, K.B. (2005). Researching Internet-Based Populations: Advantages and Disadvantages of Online Questionnaire Research, Online Questionnaire Authoring Software Packages, and Web Questionnaire Services. *Journal of Computer-Mediated Communication*. [doi: 10.1111/j.1083-6101.2005.tb00259.x](https://doi.org/10.1111/j.1083-6101.2005.tb00259.x)


Writer, S. (2015). *How much it costs to open a fast food franchise in South Africa*. Retrieved from: <http://businesstech.co.za/news/business/88582/how-much-it-costs-to-open-a-fast-food-franchise-in-south-africa/>


Zama, W. (2017). *The Role of South African Financial Institutions (public and private) in the Development of SME's and Entry Level Black Entrepreneurs in South Africa: Comparative Analysis with Respect to India and Brazil*. (Masters Dissertation). Johannesburg: University of Witwatersrand.

APPENDICES

Appendix A: Online questionnaire that research participants completed

FULL COLOUR THINKING





How franchisees raised the equity contribution required to purchase their first franchise?

1. What gender are you?

Female

Male

2. What race are you?

3. What is your current age?

4. How old were you when you purchased your first franchise?

5. What sector is your first franchise above classified under?

1

6. What province does/did your first franchise operate in? (Select one option)

- Eastern Cape
- Free State
- Gauteng
- Kwazulu Natal
- Limpopo
- Mpumalanga
- Northern Cape
- North West
- Western Cape

7. Is your first franchise purchased still in operation?

8. How long has the franchise been in operation? (Select one option).
If you answered "No" above please answer how long the franchise operated for before it shut down.

- Less than 6 months
- 6 months - 1 year
- 1 - 3 years
- 3 - 5 years
- 5+ to 10 years
- Over 10 years

9. What was the total purchase price of the franchise?

- R1-R100 000
- R100 001 - R300 000
- R300 001 - R500 000
- R500 001 - R750 000
- R750 001 - R1 000 000
- R1 000 001- R1 500 000
- R1 500 -001 - R2 000 000
- R2 000 001 - R5 000 000
- R 5000 0001 +

10. What percentage of the total purchase price above was equity (unencumbered cash contribution)? *(Please provide the nearest estimation if necessary)*

- Less than 10%
- 11-20%
- 21-30%
- 31-40%
- 41-50%
- 51-60%
- 61-70%
- 71-80%
- 81-90%
- 91-100%

11. What or who were the sources for the equity component above?

12. How long did it take you to raise the equity capital required?
(Select one option)

- Less than 6 months
- 6 months to 1 year
- 1 - 3 years
- 3- 5 years
- 5 - 10 years
- 10- 15 years
- 15- 20 years
- Over 20 years

13. What challenges did you face in raising the equity capital required?

14. What impact did the requirement to raise the required equity finance have on the business model adopted, on personal relationships i.e. friends and family?

15. What advise with regards to raising equity finance would you give to other aspiring franchisees?

Appendix B: Tables

Table 1: Origins of franchised systems operating in South Africa in 2004

Local concepts	354	90.5%
International concepts operated either by a subsidiary or master franchisee	37	9.5%
Total	391	100%
<i>Source: Franchise Census 2004, commissioned by the FRAIN project of Namac Trust</i>		

Table 2: Franchise industry sector
Franchise Census 2004

Industry sector	Sales R million	Percentage of total sales
Automotive products and services	7 302,07	5,65%
Building and home maintenance	5 906,48	4,57%
Business to business supplies	521,99	0,40%
Education and training	615,42	0,48%
Fast food / take-out	7 894,68	6,11%
Health and beauty services	2 591,41	2,00%
Other business sectors	6 820,76	5,28%
Real estate agencies	1 923,61	1,49%
Restaurants / sit-down	3 532,64	2,73%
Retail incl. convenience stores	39 514,65	30,56%
Video rental and entertainment	448,60	0,35%
Petrol supplies	52 219,44	40,40%

Table 3: Sorbet start-up costs (Source: Sorbet website)

DESCRIPTION	NEW Salon	NEW Nailbar	NEW Drybar	NEW Sorbet Man	NEW Candi & Co
	80m2+-	60m2+-	95m2 +-	95m2 +-	95m2 +-
Design & Shopfitting	400 000	240 000	450 000	470 000	435 000
Electrical & Plumbing (Excl. A/C)	160 000	44 000	165 000	170 000	175 000
Signage	35 000	30 000	35 000	30 000	35 000
Equip/H'ware/S'ware/Comms/Sundries	160 000	75 000	165 000	165 000	225 000
Stock: Professional & Retail	280 000	115 000	295 000	300 000	245 000
Franchise Fee	115 000	115 000	115 000	115 000	115 000
TOTAL INVESTMENT	1 150 000	619 000	1 225 000	1 250 000	1 230 000
Lease deposit *	75 000	50 000	75 000	75 000	75 000
VAT	160 000	86 000	170 000	175 000	170 000
Working Capital	80 000	60 000	80 000	100 000	100 000
TOTAL CASH REQUIREMENT**	1 465 000	815 000	1 550 000	1 600 000	1 575 000
UNENCUMBERED CASH REQUIRED	735 000	410 000	775 000	800 000	790 000

* The lease deposit can vary from site to site

** The above amounts are not guaranteed and can change without any notice

** 50% of this amount should be available as unencumbered cash

** Acceptable proof of funding will be required

Appendix C: Figures

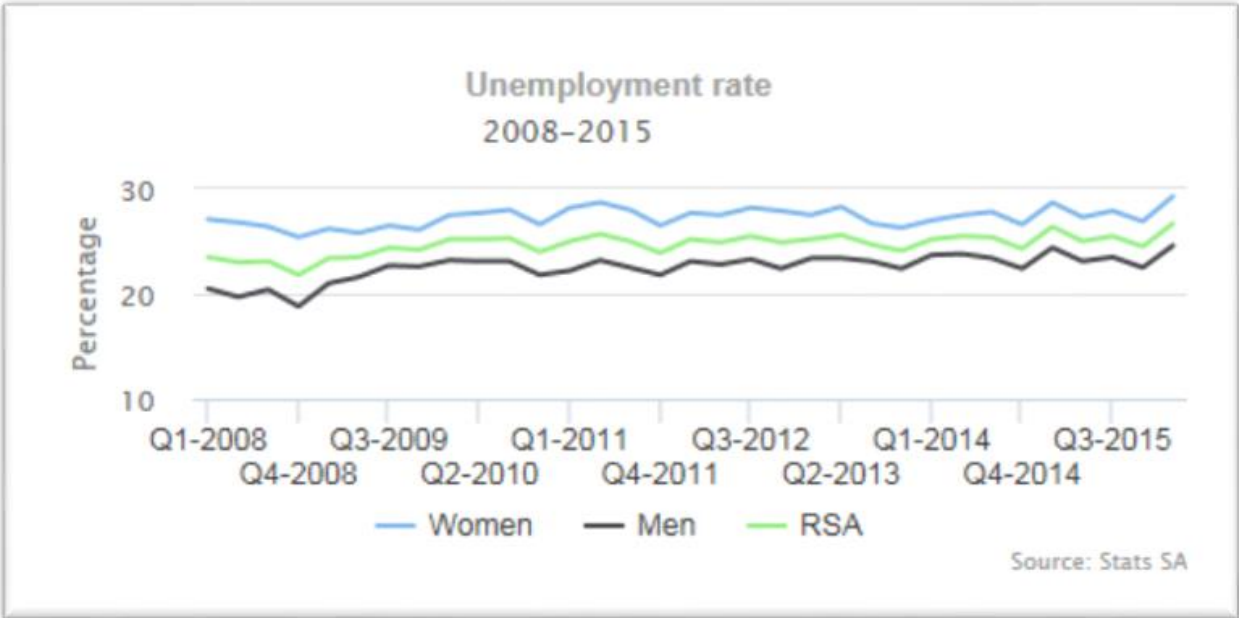
Figure 1: The South African and global economic year on year growth, 2010-2023- 2016

Region/country	2010-2017	2018	2019	2020	2021-2023
Percentage	Post-crisis	Average GDP forecast			
World	3.8	3.7	3.5	3.6	3.6
Advanced economies	2.0	2.3	2.0	1.7	1.6
United States	2.2	2.9	2.5	1.8	1.5
Euro area	1.3	1.8	1.6	1.7	1.5
United Kingdom	2.0	1.4	1.5	1.6	1.6
Japan	1.5	0.9	1.1	0.5	0.5
Developing countries	5.3	4.6	4.5	4.9	4.9
China	8.0	6.6	6.2	6.2	5.8
India	7.3	7.3	7.5	7.7	7.7
Brazil	1.4	1.3	2.5	2.2	2.2
Russia	1.8	1.7	1.6	1.7	1.4
Mexico	3.1	2.1	2.1	2.2	2.9
Sub-Saharan Africa	4.3	2.9	3.5	3.6	4.0
South Africa ¹	2.0	0.7	1.5	1.7	2.4

1. National Treasury forecast

Source: IMF World Economic Outlook, January 2019 and IMF World Economic Outlook database

Figure 2: The South African unemployment rate



Source: Stats SA

Figure 3: Key challenges facing entrepreneurs according to The Seed Academy 2016 start-up survey

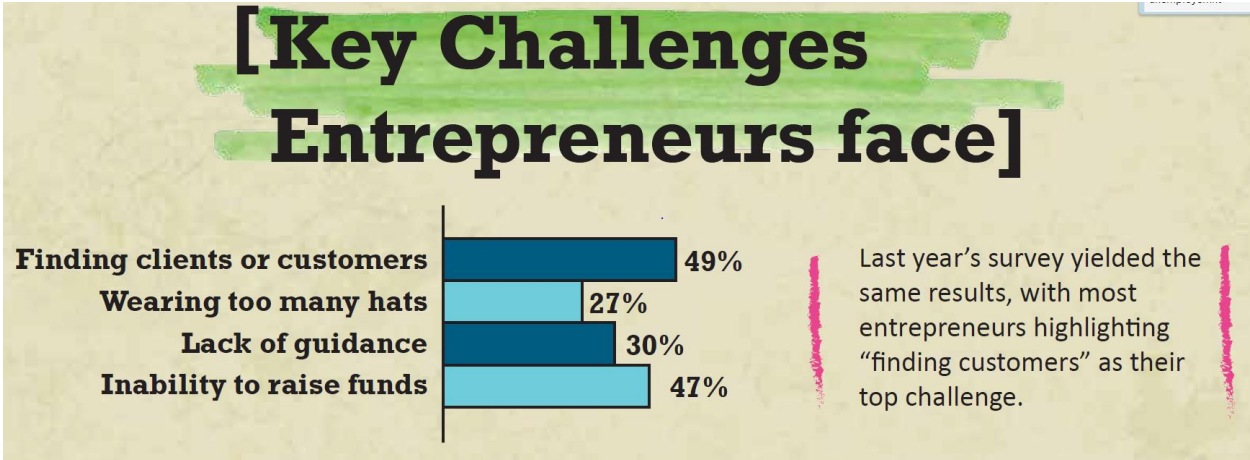


Figure 4: How entrepreneurs funded their business to date according to The Seed Academy 2016 start-up survey

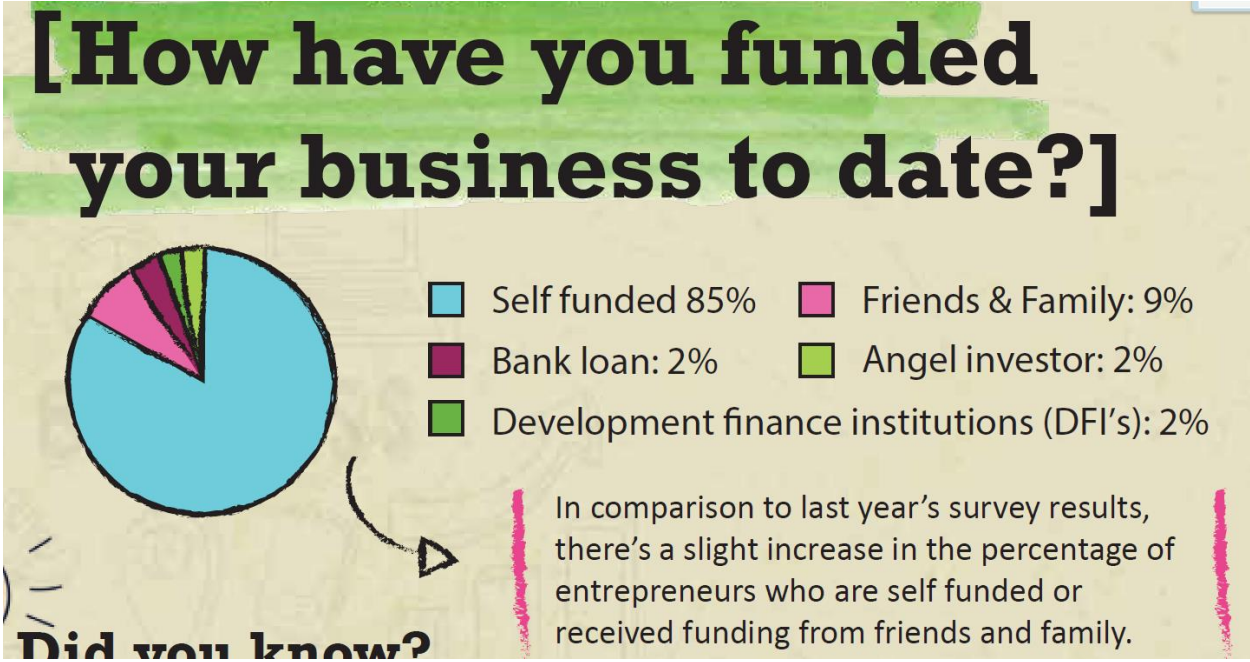


Figure 5: Franchisees annual turnover

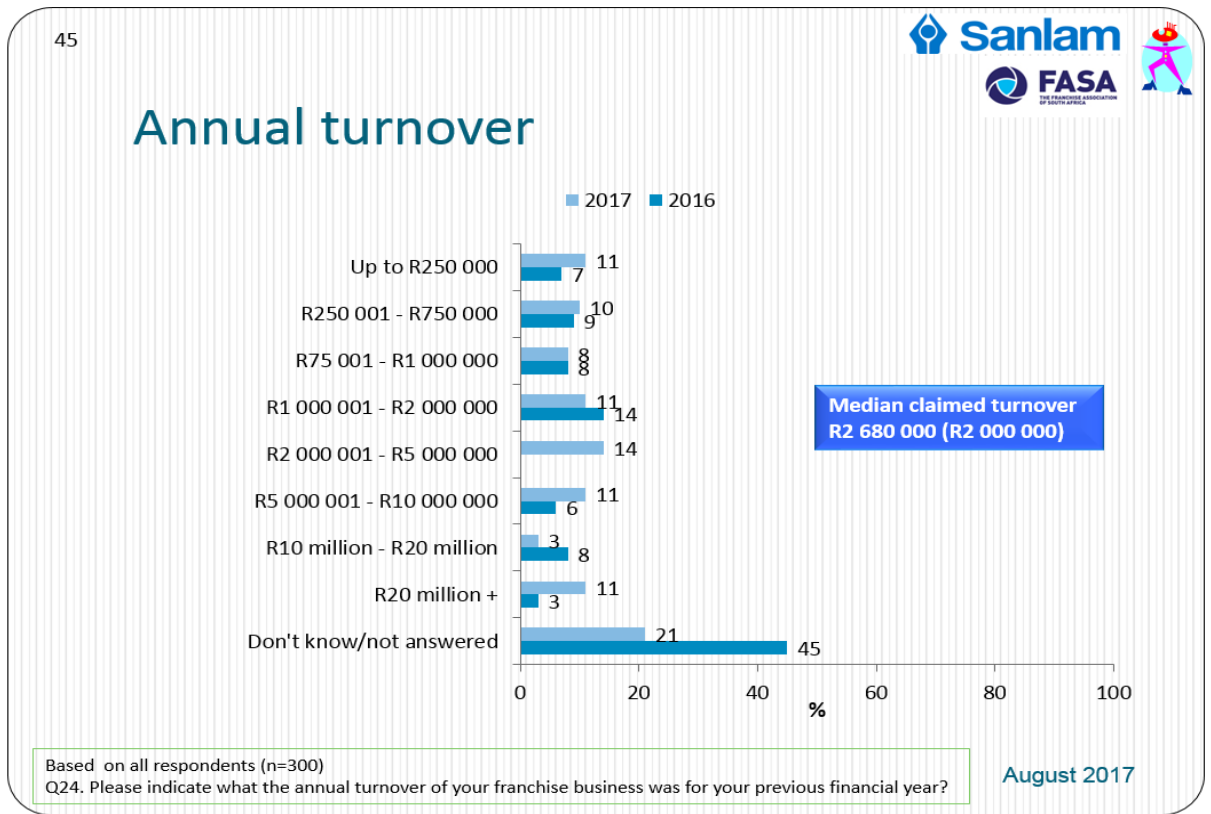


Figure 6: Franchisees time in business

